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OVERSIGHT OF DOD'S INADEQUATE USE OF OFF-THE-SHELF ITEMS

HEARINGS

BEFORE THE

SUBCOMMITTEE ON OVERSIGHT OF
GOVERNMENT MANAGEMENT

OF THE

COMMITTEE ON
GOVERNMENTAL AFFAIRS
UNITED STATES SENATE

ONE HUNDRED FIRST CONGRESS

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OVERSIGHT OF DOD'S INADEQUATE USE OF OFF-THE-SHELF ITEMS

TUESDAY, MAY 16, 1989

U.S. SENATE,
SUBCOMMITTEE ON OVERSIGHT
OF GOVERNMENT MANAGEMENT,
COMMITTEE ON GOVERNMENTAL AFFAIRS,
Washington, DC.

The Subcommittee met, pursuant to notice, at 9:32 a.m., in room 342, Dirksen Senate Office Building, Hon. Carl Levin (Chairman of the Subcommittee) presiding.

Present: Senators Levin and Cohen.

Staff Present: Linda J. Gustitus, Staff Director and Chief Counsel; Peter K. Levine, Counsel; Mary Berry Gerwin, Minority Staff Director and Chief Counsel to the Minority; Frankie de Vergie, Chief Clerk; William Luke, Majority Professional Staff Member; Warren Reece, Majority Professional Staff Member; and Melinda Loftin, Majority Professional Staff Member; Sean McAvoy, Minority Professional Staff Member.

Senator LEVIN. Good morning, everybody.

We are going to reverse the order here so Senator Cohen can meet some very important scheduling commitments, and we will start with Senator Cohen for his opening statement.

OPENING STATEMENT OF SENATOR COHEN

Senator COHEN. Thank you very much, Mr. Chairman, and I appreciate your accommodation.

I am pleased that the Subcommittee is holding this hearing today to explore a subject of great importance to the efficiency of the military procurement system; namely, the Department of Defense's record in purchasing off-the-shelf items.

Congress has expressed its will that the Department of Defense expand the use of off-the-shelf items in its procurement, and has directed the Department to identify and then take action to remove impediments that exist to achieve wider procurement of these nondevelopmental items.

The commercial market is capable of producing a broad range of quality items, such as computers, bolts, spare parts, footwear, wearing apparel, that can, with some, or even no modification, serve the needs of the Defense Department.

Not too long ago, the Defense Department's purchase of commercially available products at prices far above their usual cost made some rather big headlines. Indeed, the tales of the $640 toilet seats, the $7,600 Air Force coffee maker, and the $435 hammer are now quite legendary. But, in addition to making flashy press stories, these examples, I think, were strong evidence of how our defense procurement system was sorely in need of major reform and demonstrated that the Government was paying far too much for items that it could secure at a much more reasonable cost.

Although the worst sins of the $600 creature comforts may be in the past, there is evidence that our military procurement process is still discouraging the use of so-called off-the-shelf items.

Too often, the Department of Defense continues to subject commercially available parts to complex military specifications, requiring contractors to reinvent a unique military specification wheel when a commercially available wheel would perform the task just as well.

The effect of this problem is to drive up costs for the contractor, to limit the amount of competition in Government contracts, and ultimately to inflate the costs of military procurement for the taxpayer.

The problem of over-specification can discourage qualified and capable companies from doing business with the Pentagon. And I have learned firsthand of one example in my own State of Maine. The Maine Glove Company, which is based in Houlton, Maine, is a company that makes dress and work clothes. It supplies its gloves to civilian agencies of the Government. This company has tried to do business with the Department of Defense, but has determined that it simply is not worth the cost involved to meet the excessive specifications of DOD contracts.

The Pentagon buys dress and work gloves, but requires its suppliers to use a particular type of stitching machine that has been discontinued and is no longer in the commercial glove industry itself. In fact, I have been told that this type of stitching machines dates back to the 1920's and is used by very few mills in the entire United States.

The Maine Glove Company estimates that it could cut the cost for dress and work gloves for DOD by some 20 to 30 percent without any loss of quality, if the specifications were changed to allow other types of stitching to be used.

Mr. Chairman, we are talking about simple dress gloves here. And as my constituent put it, these are "simply four fingers and a thumb," not gloves that are used in high temperatures, combat or other special conditions that would require unique tolerances or complex modifications. Dress and work gloves provided by this glove company in Houlton are adequate for the general public and adequate for other agencies in the Government, but apparently inadequate for DOD.

Such specifications simply do not make any sense. They lock-in contracts to a few companies who can meet these unreasonable requirements, and they greatly limit fair competition.

Today we are going to hear some other startling examples of over-specifications in the Defense Department contracts. We are going to hear how packaging specifications for an O-ring makes the box itself cost $2 while the O-ring only costs 5 cents. We are going to hear about how a procurement for a part that cost $200,000 was scrapped because it was too expensive, while the packaging alone on another procurement at the very same time cost $400,000.

If these examples are at all representative of how the Department of Defense is procuring goods, then I think reforms are certainly in order.

Over-specification is not the only problem that is currently discouraging commercial vendors from doing business with DOD. We are going to hear today about other factors that are responsible for impeding the use of non-developmental items.

DOD contracts typically include contract clauses that may be unnecessary or inappropriate for commercial suppliers. Some of these clauses are standard clauses required by statutes, others by regulations, while still others are discretionary. And there appears to be little uniformity or clear guidance on which clauses ought to be included in specific contracts. As a result, some clauses place unnecessary burdens on commercial contractors who are trying to sell to the Department of Defense.

Finally, the requirement for cost or pricing data can be a major impediment to the use of off-the-shelf items in DOD procurement. There are many commercial suppliers who are ill-equipped to supply the detailed documentation of how much it costs to build the product. And they might price themselves out of the commercial market if they were to develop and maintain the accounting systems required to submit these costs and pricing data.

While DOD undoubtedly has a right, and indeed the obligation, to ensure that the costs of the items it procures are reasonable, we must review the process to be sure that unnecessary obstacles or requirements are not causing qualified commercial vendors to avoid doing business with DOD.

I would like to add only one caveat to the discussion that will take place today.

I believe strongly that we must not underestimate the legitimate need for unique military specifications for a wide range of items that have to be procured by the Department of Defense. In many instances, there is no commercial counterpart which meets the special needs of the military and defense system. We should not lose sight of these special needs.

The purchase of non-developmental items, when they meet the same quality and perform the same function for DOD is just good common sense, especially in these days of tight defense budget and looming Federal deficits.

Discouraging commercial vendors from doing business with the Pentagon through arcane specifications, mazes of cumbersome contract clauses, and excessively burdensome data requirements serve no one—not the small business which wants to supply the Government, not the serviceman or woman who could have the state of art equipment delivered faster and more easily, and especially not the taxpayer who ultimately pays for over-specified items that could be bought at a much lower price.

Mr. Chairman, again I want to thank you for accommodating me. I hope to return very soon and share in the hearings. And thank you again for scheduling these hearings.

OPENING STATEMENT OF SENATOR LEVIN

Senator LEVIN. Thank you, Senator Cohen.

In October 1986, almost 3 years ago, we enacted a law requiring the Department of Defense to purchase, whenever possible, items that are already produced instead of developing totally new items to meet its needs. Items that are already being produced are called "non-developmental items," or "NDIs." NDIs can be items already sold in the commercial world or items already in use by the Government. In either case, they can be produced without new military specifications.

Three years ago we passed this law. It required the DOD to identify and remove regulatory impediments to the acquisition of NDIs. Despite this mandate, our witnesses today will testify that not much has happened, and major impediments remain to buying non-developmental items.

It seems that the Department of Defense is still hooked on the old way of doing things, still wedded to military specifications and, we will learn today, even outmoded parts and some machining processes that have not been in use since the turn of the century.

It took us years to convince the Department of Defense that competition in procurement was key to reducing cost and improving performance. Senator Cohen and I authored the Competition in Contracting Act, and I think that has helped to finally change the Government procurement culture in that area. Now we have to do the same thing in the area of NDIs.

Many of the items that the Department of Defense purchases, the big ticket items, like missiles, submarines, and aircraft carriers, obviously have to be made to DOD specifications. They are unique and not used in the commercial world. But a huge amount of items, including many of the nuts and bolts, and even sophisticated computer equipment on such submarines and missiles are similar to those used in the commercial world, or on other government-developed equipment.

It is foolish, wasteful, and unnecessarily time-consuming for us to build items from scratch that are already being produced and have already been tested in the commercial marketplace. It leads to extraordinary examples of waste, from the $435 hammer to the $640 toilet seat to the $7,600 coffee maker, and the $9,600 allen wrench. It is like reinventing the wheel every time we get a flat. And that is not all.

When the Department of Defense finally does decide to buy commercial, it frequently tries to impose on commercial contractors all the procedures and requirements that we developed to protect ourselves when we purchase military-unique systems.

DOD requires special monitoring, auditing and testing for military-unique systems. These procedures are clearly necessary when we purchase systems that have not been tested with commercial sales. However, many of them are totally unnecessary or inapplicable to commercial products, but that does not stop the DOD from frequently imposing them anyway.

These special requirements cost a contractor time and money and, therefore, it costs the Defense Department and the taxpayer time and money. We should use them when necessary, but we should avoid them when we can. And today's hearing will demonstrate that the Defense Department often imposes these costly burdens without justification.

The first problem that we will hear about is overly rigid and detailed military specifications for the purchase of widely available items that could be purchased off the shelf.

The second problem is burdensome regulations, contract clauses, and duplicative and unnecessary procedural requirements that discourage commercial sales even in cases when the Government does decide to buy a commercial product.

With regard to the first issue, over-specification, we will hear testimony that the Army has been imposing detailed military specifications that are 20 or 30 years out of date, on widely available commercial auto parts. In one case, DOD's specifications are so absurd that the Department of Defense would require a 5-cent brake part—may I add a non-fragile 5-cent brake part—to be packaged for delivery in a $2 box.

In another case, the Air Force refused to purchase an automatic parachute release mechanism that has an accident-free record in extensive use by the air forces of Canada, West Germany, Italy, and Spain. Instead, the Air Force decided to develop an entirely new release mechanism at three times the price of the proven device and at an unknown performance risk.

The Air Force argues that the existing device does not meet all of its requirements. But, despite repeated inquiries by the Subcommittee staff, the Air Force has yet to produce any document showing where these requirements came from, or how the Air Force justified the need for these requirements and the resulting expense.

These are not isolated examples. For example, the Subcommittee has learned that the Government specifications for hand towels is 18 pages long and require a precise weave, number of stitches, measure of shrinkage and absorption rates. The military specifications for gloves require specific machinery that was used in the 1920's and has not even been produced for almost 40 years.

Even when the Government does decide to purchase an off-the-shelf product, it imposes burdensome contract requirements that frequently drive away commercial sellers. One witness will testify that a prime contractor presented his company with an inch-thick contract solicitation pursuant to DOD requirements, for the purchase of two $200 testing devices. Now, that is about 30 pages of contract clauses for each $100 in the purchase order. And that does not even include the dozens of other requirements that were incorporated by reference. Understandably, the company balked at the offer and refused to sell its product to the Government.

The Subcommittee staff recently conducted a review of the contract clauses included in six separate DOD solicitations for the commercial purchase of oscilloscopes, an instrument for measuring variation in electrical current. The staff found that 171 different contract provisions were included in at least one of the six solicitations. Of these contract clauses, only 27 were included in all six of the solicitations, and only 57 were included in more than half of the solicitations. And this again is for the purchase of the very same item.

Now, that would lead one to conclude that as many as 129 of the 171 contract clauses in these solicitations were unnecessary. That is over two-thirds. And while each of these clauses are obviously easily includable in a contract, each costs a lot of time and money to the contractor, and ultimately to the Government when they are included. And when they are imposed needlessly, they just simply are a massive substantial waste.

Finally, with regard to duplicative procedural requirements, I understand that the GSA maintains price schedules for products that meet commerciality requirements and are eligible for exemption from many Government requirements. However, we will hear testimony today that the Department of Defense not only refuses to accept these GSA determinations of commerciality, but also requires every seller to the DOD to recertify and provide it the same data that has already been approved by GSA. That is absurdly wasteful. And like all these other problems, helps to deter thousands and tens of thousands of bidders from bidding on solicitation requests.

There are just too many cases of this kind, where the Department of Defense imposes requirements that it does not need, and all of us pay the extra costs. With the budget deficits that we are running, we cannot afford to ignore this kind of waste.

Today's testimony will lay the groundwork for a second hearing on June 1, when we will hear the views of the Department of Defense and perhaps other Government witnesses about the problems that are raised here.

After that, I hope that we can sit down and work out some constructive ways of reaching a common goal, which is saving taxpayers dollars through increased DOD purchases of already developed commercial and off-the-shelf products.

Our first witness today is Bob Rossow. Bob is the Director of Government Sales for Midland Brake in Owosso, Michigan. For several years now, he and Midland Brake have been trying to sell commercial brake parts to the Army's Tank and Automotive Command. And he is here to tell us today about some of the problems that his company has encountered in that effort.

Mr. Rossow, we particularly welcome you coming from Michigan, a very welcome indeed.

TESTIMONY OF ROBERT ROSSOW III, GENERAL SALES MANAGER, MIDLAND BRAKE, INC., OWOSSO, MI [1]

Mr. Rossow. Thank you, Senator.

Midland Brake is a wholly owned subsidiary of Echlin, Inc., of Branford, Connecticut. Echlin is a major manufacturer of automotive and brake and electrical system components.

Echlin is a large corporation, currently 281 on the Fortune 500 list. It is also overwhelmingly commercial. Less than 1 percent of our sales are Government related. That is largely because brake system components are not high cost items. However, we do play a significant role in our particular segment of the defense market.

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[1] See p. 97 for Mr. Rossow's prepared statement.

Other Echlin elements have much to offer also. However, when I consider the costs and risks involved in developing these opportunities against the returns, I really question whether we wish to pursue the matter.

When 1 percent of our business seems to create 80 percent of our problems, one certainly has reservations.

I am here this morning to discuss with you some of the problems Midland, as a manufacturer of commercial products for the domestic heavy-duty truck industry has faced in attempting to sell nondevelopmental commercial items to the Government.

Problem areas for a commercial manufacturer engaged in governmental contracting include specifications, technical data rights, cost or pricing data, contract management, and social and compliance programs, and we have concerns in all areas.

However, I shall largely restrict my comments to Midland's experience in the area of specifications and getting them changed.

Consumable repair parts, meaning those which are discarded rather than repaired, offer the Government an excellent opportunity to take advantage of commercially available products. Hydraulic brake system components provide a good example. In addition to Midland, four other major manufacturers produce competing products: Bendix, Delco, EIS, and Wagner. All five manufacturers' parts are identical for all practical purposes. While minor variations exist, none are significant. Since all five of us compete for the same spot on the same vehicle, we cannot be significantly different.

Unfortunately, the Department of Defense procures hydraulic brake system components by means of design specifications. Some of these even go to the extreme of specifying the direction of rotation of the helix of a spring. Many of these specifications date back to the 1940's and early 1950's and even the original manufacturer no longer makes the item to the drawings.

When Echlin purchased Midland back in 1982, it was obvious that many opportunities existed. It was also obvious that most of our products, while similar, were not identical to the technical drawing packages. Commercially, this is irrelevant as long as the product meets form, fit and function.

With Government contracting, however, such is not the case. I knew that to be successful selling our products to the Government, I had to get the specifications changed from design to performance, and thus began a 5-year campaign.

We bid on and won several hydraulic repair parts solicitations. Following awards, we submitted requests for waivers, each of which proved to be a lengthy and frustrating experience. Throughout the process, we continually asserted that these components should be procured through performance specifications. Although the engineers agreed in principle, nothing occurred. The passage of the Competition in Contracting Act and related legislation gave us the moral high ground but little else. And it was very quickly obvious that dealing with engineers and buyers was not going to be successful.

As a result, in May 1985, I wrote to General Flynn, who at that time was the United States Army Tank-Automotive Command's Deputy Commander for Procurement, proposing to him an industry-Government conference on repair parts specifications, which the General endorsed. The meeting was held in November at which time it was decided to move towards performance specifications based on SAE and industry standards.

In the meantime, the struggle continued. The Defense Construction Supply Center, which purchases many of the parts for TACOM began to issue solicitations as competitive proposals which did permit us to offer alternative offers. But need for engineering approvals remained. And, moreover, one had no guarantee that because a waiver was approved on one contract, it would be approved on the succeeding contracts. In one case, Midland, after having delivered more than 180,000 wheel cylinders for the 2½-ton truck to the United States Army without a quality deficiency report of which we are aware, was informed that our product did not meet the technical requirements.

A similar scenario occurred with respect to master cylinders. In both cases, we were the low bidder. In both cases we protested, in the first case, to the head of the agency; in the second case, we went to the GAO. In both cases, the protest was denied. And that was a little bit irritating, I may say.

In the middle of last year, some of the revised specifications began to appear. Unfortunately, during their drafting, industry had not been consulted, and so what we began to see varied considerably from standard practices. This precipitated another letter from me to General Flynn, suggesting that perhaps we ought to sit down and talk these things over again. And once again the General concurred.

The meeting was held in late January of this year, prior tc which TACOM Engineering circulated their drawings and specifications and solicited industry input. As a result, the meeting was held and was remarkably productive. We sort of had to pinch ourselves to believe that it was really occurring.

The result was a set of specifications which are realistic in terms of production, and addressed at the same time the concerns both of industry and of the Army. And I would also say their success was largely due to its Chair, Mr. Alex Sinclair of the Tank Command, who has a lot of practical experience and, most important of all, was completely unafraid of making a decision.

Although the proceeding may seem like a success story, and in the many respects it is, it is, nonetheless, a limited success. The reason is that these specifications apply to only 10 of the most visible brake system components on the largest vehicle fleets, the deuce-and-a-half and the 5-ton.

Hundreds of parts on the "cats and dogs," if you will, continue to be procured by design specifications. Whereas, the 10 covered parts are purchased in quantity, others are not, and few would tool up for half a dozen master cylinders. However, in most cases, functional equivalents are probably readily available at reasonable cost in the commercial market.

After the January meeting, one of my competitors came up to me and thanked me for getting his firm back into business. He said they had attempted unsuccessfully to do what I had done and, as a result, had withdrawn from the market, something which I had noticed, because they were quite conspicuous by their absence. That he is back is fine. I will deal with that on the bid floor. But I have to say that had the meeting not gone as it did, that we would have withdrawn from that particular segment of the market ourselves because we were just exhausted with fighting the battles.

And I want to say the war is not over. Even as I was preparing this testimony, a solicitation was issued for one of the covered master cylinders, using the old obsolete specification.

When I talked to General Flynn in February, following our meeting, as we left, he patted me on the shoulder and said "Keep them honest." And, as a result, I went out and picked up my pen and filed my protest, and it is under evaluation at this moment.

While solving problems of this sort as well as those in the other areas is a necessary condition for your reawakening the commercial manufacturers' interest in Government contracting, it is not sufficient.

A recent study reports that more than 80,000 domestic firms quit doing business with the Government between 1982 and 1987, two-thirds of those originally engaged in 1982. If these figures are anywhere near correct, we have a very serious national problem.

Why is this? I suggest it is because Government contract regulations are so intrusive, impacting every aspect of one's business, that one's firm is essentially nationalized. And no free citizen, corporate or otherwise, will tolerate this for long. And what happens is they vote with their feet and leave the market.

And so what is to be done? I suggest basically that the bureaucracy needs to be turned upside down. For better or for worse, we have institutionalized a bureaucracy that rewards conservatism, inaction and inefficiency.

There are sizable vested interests that have no desire to see changes as change represents risks. We had one individual say to us that I am here for my gold watch and I am going to do nothing to risk it.

The bureaucracy well knows that it can outlast commanders. The mind set, particularly in the lower echelons, needs to be changed. It is all well and good for a General to get up and give a charge and his troops will be out there and they will listen to him and say, "yes sir, yes sir, Garry Owen, we are going to take the hill!" And then they are going to go right back downstairs and carry on doing exactly what they have been doing for the past 20 years.

The mind set must be changed. Initiative and imagination and reasoned risk taking need to be recognized as desirable professional characteristics for the Contracting Officer, and promptly and publicly rewarded. The Contracting Officers need to learn to exercise their authority and challenge the experts who have a vested interest in seeing that things are complicated.

Unless the presently held institutional values are changed, I feel nothing will happen short of Congress disestablishing the organization.

Last, and by no means least, if the Government wishes to avail itself of commercial products, they must convince private industry that it wants to do business with the Government. Even if the Government were to commit to reducing micromanagement, professionalizing the bureaucracy, and to improving specifications, would industry believe it? Probably not, because they have heard all of this before many times.

Administrations come and go, and all have their buzz words and their special programs, many of which seem to be the old programs upon closer examination. And buzz words and reorganizations are a marvelous way of giving the illusion of doing something when actually the essence remains the same.

I feel that industry wants deeds, not words. And sort of a last comment is that my impression from reading is that foreign governments tend to consider their industrial bases as national assets whereas, here, particularly with DOD, we are treated as adversaries. And that may not be the intention, but that is the perception, and perception is reality. And life is long enough and complicated enough without going out and deliberately courting more problems.

Given the complexities and risks involved in Government business, the question is who needs it? In that regard, I would like to thank you, sir, for the opportunity to come and express our views, and at this point I would be happy to entertain any questions you may have.

Senator LEVIN. Mr. Rossow, thank you for coming forward. Your testimony is eloquently put forward. There are some real nuggets in there that I hope we all soak in in terms of the number of contractors who have simply left the market, voted with their feet as you put it. We are not sure it is two-thirds. We know it is a huge number; it could be two-thirds.That means that a huge percentage of potential competitors are not competing, and that is going to increase the cost of these products to the taxpayers.

You have given us some examples, both in your testimony and in your conversations with staff. I want to make reference to one of them, and that is a letter, which you wrote in December 1988, relative to a particular test specification, the mud slurry test. This test was suddenly devised for a particular part, which I understand had been provided for a long, long time. And the DOD came along and, after 25 years of procuring this part, decided that it would have a new design spec and that would be a mud slurry test, and here is what you wrote them:

"Why this was necessary after 25 years or so of procuring the part is unclear. While the intent of the test is obvious, it was unfortunately not carefully written. As a result, after the wheel cylinder has been submerged 78 inches deep in a mud slurry, the QAR"—what is the QAR?

Mr. ROSSOW. That is the Quality Assurance Representative, the inspector.

Senator LEVIN [continuing]. "The inspector is required to strip to his skivvies, put on his goggles, dive into the mud, swim down 6½ feet to the cylinder, peel back the boots and check the mud in the cylinder."

And you wrote parenthetically that you would pay to watch that. [Laughter.]

Mr. ROSSOW. Right.

Senator LEVIN. The Government was paying to watch it too.

And then you wrote: "I submit that barring the intervention of the Almighty, that they will indeed find mud in the cylinder, which is grounds for rejection."

Now, Mr. Rossow, did the DOD really write that requirement? Did you make that up to give us a little levity here this morning? [Laughter.]

Mr. Rossow. No, sir. That really was written by their—they have a special technical contract with one company that handles these sorts of things and——

Senator Levin. Did they change that test finally?

Mr. Rossow. That has been changed.

Senator Levin. Someone persuaded them to change that test?

Mr. Rossow. Yes, sir.

Senator Levin. In your written testimony, you mentioned another example of over-specification, which is astonishing.

You said that, under the existing military specs, that you were required to package a 5-cent center O-ring in a $2 box. Now, let us make clear what we are talking about.

Is this just a simple piece of plastic?

Mr. Rossow. This is the offending item right here.

Senator Levin. And is that a normal commercial item?

Mr. Rossow. Basically, yes. We manufacture many components of this sort for different products that we make. The item has a material cost of roughly 4 plus cents.

Normally, commercially, you would put this in a plastic bag and have a little piece of paper in there giving part number and our identity and so forth.

What the specification calls for is putting it in the plastic bag with a piece of paper identifying it, drawing the vacuum, putting that in a box, with a lot of these little styrofoam chips protecting it, putting that box inside a plastic—wrapping it in plastic and drawing the air out of that and then putting that in another box and shipping it off, which is rather impressive for a small piece like this.

Senator Levin. Is that not a fragile piece?

Mr. Rossow. No, sir. You can squeeze it, do all sorts of things to it.

Senator Levin. And what is it used for?

Mr. Rossow. I am not certain what particular end item this is a part of, but it would be for keeping fluid from going past this or any——

Senator Levin. But is that for something like a truck?

Mr. Rossow. It would be a brake system repair part.

Senator Levin. Quite typical to a commercial part?

Mr. Rossow. Normally, we sell them in quantity packs to distributors and things that—I think you have the 10-unit pack, and then you have got a 100-unit pack.

Senator Levin. Are you aware of any unique military requirements that would require this kind of extra expense for the packaging?

Mr. Rossow. None at all, sir.

Senator Levin. Can you think of any reason that commercial packaging would not be appropriate for the military in this case?

Mr. Rossow. None at all.

If I might interject, we have also seen the situation whereby demanding their specifications, they are making it difficult for them to get parts they critically need.

A case in point is the compressor on the 2½-ton truck which is currently in extremely short supply. Because of the requirements of Mil. Standard 2073, the new packaging level which they were requiring requires us to obtain a rather expensive and hard to get wood to a particular Federal specification.

For years, they have procured this in a plain cardboard box, heavy-duty. It is protected in the box. And they have been doing that since Moses was a pup, since the 1940s and never had a problem. All of a sudden, they have to have this new packaging specification. The result is that, although they need these parts, it is going to take them an additional 45 days or so to get delivery because of the difficulty in obtaining this wood. But will they change it? No, they will not. But they keep on screaming at us to speed delivery.

And it also increases the cost. The commercial boxing is roughly $2 or $2.50. The special packaging for 2073 is somewhere in the vicinity of $8.70. So we have a $6 increase in cost in the packaging.

Senator LEVIN. And what was the cost of the part in that instance?

Mr. ROSSOW. For that particular part, the prices are $163. It is a compressor, but it is the same sort of packaging that we provide to all our commercial manufacturers, truckstops across the Nation.

Senator LEVIN. In the case of that O-ring which you held up, as I understand it, that 5 cent O-ring had to be put in a box which cost about 40 times as much as the O-ring?

Mr. ROSSOW. That is about the case, sir.

Senator LEVIN. But a $2 box?

Mr. ROSSOW. Right. The packaging specification was on my crusade on the hydraulic specs. But the packaging is sort of, I feel, my next crusade, because some of these are so really ridiculous.

The case of the foam in place packaging is another area which I find very difficult.

Senator LEVIN. Would you just tell a bit about that foam in place packaging requirement?

Mr. ROSSOW. Yes, sir. Basically, in foam in place, you take the item which you are going to package, and you put it into a box, and you put this liquid in there which sort of foams up and surrounds the whole package and holds it very securely in place.

It is also a very expensive way of doing it. For air hydraulic units which we manufacture, the differential cost between the standard heavy duty commercial boxing and foam in place is roughly $10.50.

Now, we have had solicitation of up to 30,000 units. So you can figure out very quickly you are talking about almost $400,000 worth of incremental increase in costs for that particular type of packaging.

Senator LEVIN. And do you know of any military reason for it, any requirement that the military has that would justify that kind of requirement?

Mr. ROSSOW. If you were to put it in long-term storage, yes, it might be useful to have it there because of that. But these items are used rapidly. They do not remain on the shelf long and, for that reason, I really think the commercial boxing which would include waterproof type boxing should be adequate for the time it is going to be on the shelf.

Senator LEVIN. As a matter of fact, are you familiar with instances where that foam packaging is just thrown away before the part is even stored?

Mr. Rossow. Yes. sir.

Senator LEVIN. Because of space limitations?

Mr. Rossow. Right. When you go out in the field, the parts vans and trailers used in company or battalion level maintenance, have a very limited amount of space. The cube on this part is very large, and you just do not have the space to put it.

So, very frequently, what will happen is that they will open up the box, take the item out, put it on the shelf and throw the box away. And so the investment in packaging is completely lost anyway.

Senator LEVIN. Have you ever told the Department of Defense that their requirements are just too burdensome and urged them to go to a competitor, just basically said, look, we just cannot afford to comply with all of this bureaucracy. Here are the names of some competitors, or just go to my competitors and leave us alone?

Mr. Rossow. Well, not the Department of Defense directly, but a prime, and we are going through that exercise at this moment. I would cheerfully give him the business.

The problem that we are dealing with is trying to recreate, basically as an exercise in art for art's sake, a situation on technical drawing packages that existed about 9 years ago.

The problem is that the part involved is one which is covered by the new performance specifications of which everybody is aware. And these problems could be very easily resolved by simply modifying the contract to allow the use of the new product or the new specification, which covers all the problems. And rather than having to go to and try to determine intent and discover documents that are way back on clay tablets. We, unfortunately, are still wrapped up in that, and Lord knows what it was. But I told my competitor, or told my customer, "you know, hey, you know, there are other sources for this part and why do you not go talk to them?"

I knew a materials manager who was so frustrated by this whole process down there, he told me he would almost rather have AIDS than have a Government contract. He is at wit's end. [Laughter.]

I am not popular in Iola, Kansas. [Laughter]

Senator LEVIN. I do not think anybody could add anything to that. [Laughter.]

So I will not try. I guess the bottom line is we have out-of-date specs for instances that it costs more money to meet the spec and we end up frequently with a worse product.

Mr. Rossow. Right.

Senator LEVIN. Mr. Rossow, we are grateful for your coming forward. We are going to do everything we can to change this situation.

We tried a few years ago. We thought we made some progress with an amendment which required greater use of NDIs. It obviously has not taken. Not only your testimony, but lots of other testimony is going to illustrate that we did not succeed the way we wanted to with our last effort, and much greater efforts are necessary.

When you said in your opening statement that 1 percent of your business creates 80 percent of your problems, I hope that all of us, not just in the Congress, but all of us in the Administration, the bureaucracies, the agencies are listening to what you are saying. There is just no excuse for that. And we are going to try again to change it.

Thank you so much for coming.

Mr. Rossow. Thank you, Senator.

Senator LEVIN. Our next panel includes Naomi Williamson of Honeywell Inc., and B. Dan Pinick of the Boeing Company.

Ms. Williamson is the Contracts Manager for Honeywell's Business and Commuter Aviation Systems Division.

Mr. Pinick is a Senior Vice President at Boeing, with an extensive background in contract issues. And both are witnesses on this panel. Ms. Williamson and Mr. Pinick are testifying on behalf of the Electronic Industries Association.

Mr. Pinick, Ms. Williamson. Well, I guess we will go alphabetically. Mr. Pinick.

Senator LEVIN. You have heard that before, have you not, Ms. Williamson? With a W, it does not help very much.

Ms. WILLIAMSON. I could never see the blackboard in school. [Laughter.]

TESTIMONY OF B. DAN PINICK, SENIOR VICE PRESIDENT, THE BOEING CO., SEATTLE, WA[1]

Mr. PINICK. Thank you.

My name is Dan Pinick. I am a Senior Vice President of the Boeing Company, and President of Boeing Aerospace and Electronics.

Today, I am here representing the Electronics Industry Association.

I am pleased to be here this morning to discuss some of the impediments to the acquisition of commercial products by the United States Government. I believe industry, Congress and the DOD agree that appropriate use of commercial and other non-developmental products by the Government to fulfill Government requirements could significantly reduce the cost of those requirements, reduce acquisition time, and provide operationally-proven quality items for Government needs.

The benefits of using commercial products have been studied as early as 1972, as late as 1986, when the President's Blue Ribbon Commission on Defense Management, the Packard Commission, recommended the expanded use of commercial products and "commercial-style" competition in the defense procurement process. Thereafter, as you indicate, the 99th Congress enacted a law requiring a "preference for non-developmental items," and the fiscal year 1989 Office of Federal Procurement Policy Reauthorization Act included a requirement to establish an advocate for the acquisition of commercial products.

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[1] See p. 108 for Mr. Pinick's prepared statement.

Therefore, I will not dwell on the benefits of using commercial products on the assumption that their utility has been recognized. Instead, I will focus on several problems that need to be solved before these benefits can be fully realized.

Before going any further, I would like to explain the dual marketplaces served by the Boeing Company. First, the Boeing Company is the largest producer of commercial aircraft in the free world. Currently, about 70 percent of our sales is to commercial customers. At the same time, the Boeing Company is a major defense contractor. We are traditionally 1 of the top 10.

For the most part, our Government effort is separate from our commercial activity. Our Government divisions do business with the Government and have the resources and the expertise in place to comply with the military peculiar requirements in Government contracting. Our Commercial Airplanes Division has supported the sale of military commercial products in the past, such as 707s for AWACs and E-6, 747s for E-4, Air Force One, and NASA's Space Shuttle Program. We would like to continue selling commercial aircraft to the Government because we believe our commercial products offer many benefits in terms of quality, performance, availability, and price.

We have experienced, however, significant problems in our Commercial Airplane Division when supporting the sale of commercial aircraft to the Government. One of the most significant problems is the flow down of Government contract terms and conditions to our suppliers. Many suppliers to the Boeing Commercial Airplanes are commercial companies or divisions who do no business with the Government. The relationship we have with these suppliers have existed for many years, and we look upon our suppliers as our partners and an arm of our production capability. These long-term partnerships have resulted in our mutual success in producing innovative high-quality commercial aircraft at prices established by the competitive commercial marketplace.

Many of these suppliers are accustomed to operating only in the commercial world using commercial business arrangements and are not inclined to reorganize themselves to do business with the United States Government.

Now, under the current Government acquisition system, when we receive a contract for commercial aircraft, there are many Government peculiar terms, conditions and specifications that are required to flow down to subcontractors, vendors and suppliers. In many cases, the requirement to flow down these find its origin in United States statutes. In some cases, such as cost or pricing data, there are exemptions that may be available for commercial products. However, qualifying for these exemptions is often difficult and, as a practical matter, may not be available. Moreover, the myriad of remaining clauses and Government specifications are generally unacceptable to our commercial suppliers because they are organized to produce and sell their products using commercial business arrangements.

These flow down requirements are a particular problem because of the way in which commercial programs are developed. In a commercial environment, the selection of sources and the acquisition process for raw materials, parts, subassemblies, and components is set in motion and often completed well in advance of the orders being placed by our commercial customers.

The Government order for an airplane containing flow down requirements cannot, therefore, in many instances, be complied with after the fact by our vendors and suppliers. As I indicated, in most of these cases, there is no practical waiver or deviation authority for commercial products. And even where waiver and deviation authority is available to the DOD, there seems to be a general reluctance to pursue these waivers and deviations, especially where the procuring activity is required to elevate the matter to the head of the agency. Now, taken to their extreme, flow down requirements can create an absolute barrier to the purchase of commercial aircraft and commercial spare parts.

Furthermore, the problem does not end with the delivery of the aircraft. It continues for many years because of the Government's spare parts requirement to support the aircraft.

Now, Boeing's recent experience in attempting to sell a commercial aircraft to the Government was our bid for the Navy's Long Range Air ASW Capability Aircraft called the LRAACA. Boeing's proposal for the aircraft was based on the use of a modified version of the 757 commercial jet. At the time of the proposal to the Navy, the 757 was a program that had been in existence for about 10 years. This means that Boeing's network of suppliers and vendors supporting the 757 was firmly established with contractual arrangements in place.

For this reason, Boeing proposed that certain Government clauses and specifications typically applied to new Government designed aircraft be waived. Boeing anticipated that this approach, which met or exceeded the Navy's operational requirements, would allow the Navy to benefit from the advantages offered by the 757's established commercial production and supplier environment.

Nineteen Federal Acquisition Regulation clauses, a list of which is attached, were identified by Boeing as requiring flow down, and in order to comply with all the Government flow down requirements, would have meant reopening and attempting to renegotiate approximately 3,900 vendor contracts, most of which had been in place, as I said, since the beginning of the program.

Now, for a recommendation, we believe there is a large base of high-quality commercial suppliers to which the Government may not have access because of the terms and conditions associated with Government contracts. Ideally, Congressional preference for the acquisition of commercial products and non-developmental items could, to a large measure, be achieved through meaningful regulatory reform. However, it simply has not occurred.

Therefore, we perceive a need for a new legislation permitting the acquisition of commercial products with the standard commercial terms and conditions used by the manufacturer of the product.

Recognizing this is a major department from policies that currently exist, that there may be concerns regarding such a dramatic change, perhaps a trial program could be established, with results to be evaluated following a reasonable period of time. To accommodate that program, I recommend the creation of a Commercial Procurement Authority whose office could be empowered to specifically and exclusively utilize the enabling commercial products legislation. In this way, the interest of the Government would be protected, the program would be controlled, and the results known without having permanently changed the entire Government acquisition process.

One possible approach to the problem is to statutorily provide for waiver of flow down requirements where the product has met the test of "commerciality" on the same basis as for obtaining an exemption from the requirement to submit cost or pricing data. It is already recognized under current law and regulation that if a product has a price that is "based on established catalog or market prices," and is sold in "substantial quantities" to the "general public," the Government need not require the submission of certification of cost or pricing data. In turn, it appears logical that the manufacturers of this same commercial product should be equally relieved of other obligations that are inconsistent with commercial terms.

Critical to this approach, however, is the need to further identify, further clarify and broaden the current definition of what constitutes commerciality of a particular product. This can be done by redefining some of the terms having to do with commerciality in the current FAR.

Some other recommendations: Short of broad legislative authority initiative, there is no way to completely fix this problem. However, let me suggest some changes that could make a difference even under existing law.

First, appropriate language could be added to the FAR which recognizes that in those situations where the Government acquisition includes materials, parts, subassemblies and components that have been routinely produced and ordered by a manufacturer as part of its ongoing commercial activities, the suppliers and vendors of the prime should not be considered subcontractors for purposes of flow down of Government terms and conditions. This would help eliminate this after-the-fact imposition of those flow down requirements.

Second, when commercial sources are known to exist that meet Government requirements, the Government's acquisition plan should encourage the services to use all available waiver authority requested by the prime and its suppliers and vendors of commercial products.

Third, the DOD should establish Commercial Products Advocate to work with the OFPP Advocate which was required by the fiscal year 1989 OFPP Reauthorization Act to:

Review all proposed procurement regulations to determine those which encourage or discourage the acquisition of commercial products.

Provide recommendations to the Secretary of Defense and the Administrator OFPP, as to what statutes and procurement regulations should be rescinded or modified to encourage the acquisition of commercial products.

And, finally, provide recommendations as to methods for simplifying procurement regulations governing the acquisition of commercial products.

Now, in conclusion, I would like to again point out that, in my view, without statutory enabling language which, while preserving other public policies, creates a vehicle for awarding Government contracts for selected commercial products using the terms and conditions and specs that are used by the manufacturer of the product in the commercial marketplace, the Government will not adequately benefit from the use of high quality commercial products at competitive prices.

Thank you very much for providing me the opportunity to present our views on this important issue, and I would be pleased to answer any questions you may have.

Senator LEVIN. Thank you very much, Mr. Pinick.

Ms. Williamson.

TESTIMONY OF NAOMI M. WILLIAMSON, MANAGER, CONTRACT MANAGEMENT, BUSINESS AND COMMUTER AVIATION SYSTEMS DIVISION, HONEYWELL INC., GLENDALE, AR [1]

Ms. WILLIAMSON. I represent the other side of the story told by Mr. Pinick. We were in the subcontract position in the procurement.

I am representing the Business and Commuter Aviation Systems Division of Honeywell. We sometimes call that BCASD. So if you hear me use that acronym, that is what it means.

The Business and Commuter Aviations Systems Division is a part of the Commercial Flight Systems Group of Honeywell. The group is the world's leading supplier of avionics to our served markets. That those markets include air transport aircraft, commuter aircraft, business and executive jets, turbo props, and helicopters.

We serve most of the world's original equipment manufacturers and users of avionics.

We are subject to operational and safety requirements of multiple airworthiness authorities worldwide, like the FAA. The way we develop our products are on internal funds, and we recover the price of development through a pricing structure which has to be competitive for us to maintain our market share.

As a typical commercial contractor, we assume the risks and produce product independent of Government specifications and funding. We do not actively pursue Government business in our division, although Honeywell has substantial Government business. But we do respond to Government solicitations when we are asked. And in this particular instance that is what I will be talking about.

We strongly support the Government's initiatives towards Government purchase of non-developmental items and commercial products where that kind of purchase can fit the needs of the Government.

Our products include the latest state-of-the-art sensors, controls and cockpit displays such as automatic flight control systems, inertia reference systems, and electronic flight instrument systems.

Our experience on the LRAACA program, which Mr. Pinick referred to as the Long Range Air Anti-Submarine Warfare Capability Aircraft, was in pursuing with Lockheed a subcontract for the avionics for that aircraft. We started that effort in 1986 and had estimated that for the division the program would be worth over

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[1] See p. 119 for Ms. Williamson's prepared statement.

$200 million. That was in Navy sales, foreign sales, as well as retrofit sales.

After the first rounds of competition, Honeywell BCASD was selected as the preferred supplier for the avionics subsystems for the aircraft based on our presentation of a proven state-of-the-art Gulfstream cockpit displays and several other systems.

We proposed five total systems in the long run. We were going to take the technical risk of integrating those systems for Lockheed and the Government and put that proven technology on the aircraft.

Our Honeywell engineers were put on site to help Lockheed prepare the avionics proposal to the Navy. And as a result, our avionics were pictured on the front of each volume of Lockheed's proposal to the Navy.

The Navy also visited our facility and reviewed our products and the Gulfstream IV simulator, the test-pilot flew on the simulator and the Navy Program Manager visited, so they were quite aware of Lockheed's effort with regard to purchasing commercial avionics for that program.

Lockheed wanted to make sure that they could qualify for the competitive exemption from certified auditable cost and pricing data, and therefore made sure that they kept our competitors in until the best and final offer.

Honeywell's management made the very difficult decision to withdraw from such a large chunk of business after Lockheed won the program using our avionics design in their proposal, but before Lockheed had formalized the subcontract award and negotiated the subcontract with us.

I am going to back up a little bit and clarify why our division bid on this program, as opposed to one of the military avionics divisions.

Lockheed specifically asked us to bid because the Navy had specified that they wanted the bidders on the prime contract to consider commercial electronic flight instrument systems. Lockheed had had experience with us on the C-130 program with our particular division and had a good experience. Therefore, they came to us and asked us to bid the program.

We were immediately concerned with the issue of Government flow down terms and conditions, because we were aware of that as a problem, but we got together with Lockheed, had some meetings and discussed the issue, and we read the Packard Commission report, and we also read the Government's publications on the preference for nondevelopmental items.

As a result, both Lockheed and Honeywell determined—or decided that the environment was ripe for the Navy and the Government to purchase commercial avionics for this application, as opposed to avionics that would have to be developed from the ground up.

The role I played in this particular procurement was in the early working level meetings with Lockheed where we discussed the requirements for commercial contracting terms and the Government initiatives on commercial contracting.

It was not until the procurement reached the final stages of competition in May 1988 that Lockheed said, you have to respond, clause-by-clause, to the Government Terms and Condition Military Subcontract, and the reason they gave for doing that was because we were, as one of the competitors, our competitors were military contracting types, and they wanted to make sure that they kept it so that both of us had responded to exactly the same request for proposal in terms of evaluating the proposals.

It was at that point that I called the corporate contract management staff and the Office of General Counsel, which is a resource I do not believe most commercial contractors have available to help them if they get to the point where they have to respond at the request of a customer to a Government contract. There certainly was no one within our division who had any current expertise in dealing with the Government procurement process.

So why did we eventually withdraw our bid? Essentially, we determined that the risks were too great and too many. First, and most importantly, was the requirement for the imposition of cost and pricing data. Our understanding, after we analyzed the regulations, was that those were mandatory, statutorily required items that could not be—that Lockheed did not have the choice not to pass to us.

We had analyzed the contract for the likelihood of the imposition of cost or pricing data requirements over the life of the program, and even though Lockheed had kept the procurement so that the competitive exemption would apply at contract award, over the life of the program we saw many particular instances where the cost and pricing data requirements would come into the contract.

The three major entry spots for cost or pricing data requirements were—the first was in the follow on or option exercise area. The contracting officers for the Government have the choice, on an option exercise, to require new cost and pricing data. They do not have to take firm fixed price options at the firm fixed price.

The second area was in the procurement of spares directly by the Navy. We would have had no way to support direct purchases by the Navy, because we could not qualify for the standard form 1412 exemption. And the third area was in the area of changes, where if you do changes, you must supply certified cost and pricing data.

Lockheed submitted, on our behalf, a request for waivers to the Navy for the cost and pricing data elements that were in their contract. It is not clear whether those waivers would have helped on the issues of spares and options, but it would have helped on the issue of changes. I never saw a final response from the Navy on the request for waivers, but was told by Lockheed just last week that it was turned down.

We had proposed alternatives in our proposal to protect the Government on places where those protections, based on initial competition, would have failed. For instance, for firm fixed price options, we made it so that there was a firm fixed price option with an escalation clause that would be capped by our commercial catalog and for prices for similar products. That way, as we continue to develop new products that had the same functions, we would have passed onto the Government the competitive pricing influences that affected our original prices to Lockheed.

We also proposed a reasonableness fact finding clause for the changes issue and offered to sell the Navy spares directly to Lockheed at the OEM price.

One of the things that we did after—when we were considering taking this contract, we did an internal study on what differences there are between a military division in terms of overhead personnel and a commercial division in terms of overhead personnel.

I have one example statistic here today, and that is just the ratio of professional accountants it takes to run a Government contract system versus a commercial contract system. The ratio of accountants is 4 to 1 in Honeywell—I have to clarify. This is between the military avionics division and the commercial aviation business.

One accountant in our commercial business handles about $10.9 million worth of business versus one accountant handling about $3.1 million worth of business in our military division. So the cost to us is significant if we have to supply that kind of support.

With regard to terms other than cost and pricing data on the contract, the other ones that particularly concerned us were all the other audit type clauses, like audit of quality and source inspection that would allow the Government to come in and close down our production line, which would be producing both the commercial market's product and their product.

We were concerned about design data rights. We did have some applications—engineering non-recurring quoted to Lockheed, and we were concerned that we would not be able to protect our basic design rights.

We could not handle the tooling and sourcing, reporting, all of the administrative kinds of clauses that change the way we do business. We could handle it, but we were not willing to change to handle it.

The 1412 standard form exemption did not apply for many of the instances we had put down, because it does not apply for modified product and new products. It does not apply if there are too many sales to the Government. It does not apply if there is not enough variety of commercial customers, and in this case, many of the products we sold, we sold only to Gulfstream. It also does not apply to products not sold at catalog, depending on whether the auditor will accept a distribution around the catalog price.

The risks we identified were the eventual imposition of cost or pricing data at some point to both us and our vendors, including our other divisions. The 8 by 8 display was a part of the proposal. It was actually produced by another one of our divisions, and the cost or pricing data requirements would have flowed to them as well.

We were also concerned that since the Business and Commuter Aviation Systems Division does not do military business, we do not have the complete infrastructure for compliance with all of the regulations, and as we got smarter in going through all of the regulations, we realized how many there were that we just did not have the structure to comply with.

We also could not disrupt our subcontracts with suppliers that had long-term commitments.

There was some support of the Navy concerns. We offered a standard commercial warranty. They seemed uncomfortable with the idea of not being able to get data for repair in their own place.

Because Lockheed was asking us to negotiate from the military contract as a base, as we got into the analysis, we just concluded that their way of looking at the world was so different from ours that to try and put our view on that whole contract and make it work for both of us, just could not be done.

So in summary, our biggest issue is to eliminate the requirement for certified cost or pricing data in appropriate circumstances, and where there is a reasonable substitute for audit, to ensure that the Government is getting a fair price, in the commercial arena. We think this can be established.

Fair prices can be established by looking at the market and analyzing what a reasonable person would pay for an avionic system, and our recommendation is that when the Congress addresses this, they not do it piecemeal in the sense that if they address one of the issues, all the rest of them go away.

Military contracting is a whole way of life. If you are going to get the benefits of the commercial price, you cannot require conversion to the Government way of doing business.

Therefore, we agree with the recommendations of the Association that there should be a set of commercial terms and conditions that the Government finds acceptable to use to buy commercial products, and in the short-term, the main issue is addressing the cost or pricing data issue.

Thank you. We will be pleased to answer any questions.

Senator LEVIN. Thank you, Ms. Williamson.

Mr. Pinick, first let me ask you some questions.

You described a problem that you had with a particular kind of a Navy anti-submarine aircraft. As I understand it, Boeing is set up to comply with Government contracting requirements, but your commercial subcontractors cannot. Is that basically right?

Mr. PINICK. A lot of them cannot.

Senator LEVIN. And if you had won that LRAACA competition, how would you have dealt with that problem? You said that you had about 3,900 contracts you might have had to reopen.

Mr. PINICK. Our proposal included a commercial practices provision which recognized this problem and would have permitted us to continue with our commercial subcontractors without change. We had simply conditioned the proposal on retaining our commercial practices for that part of the program—the commercial part.

Senator LEVIN. So you would not have had to reopen your contracts?

Mr. PINICK. That was the condition.

Senator LEVIN. It was a condition that you not be required to do that?

Mr. PINICK. That is correct.

Senator LEVIN. All right. Now, you have had some of the same difficulties with regard to other modified commercial aircraft that you have sold to the Government, as I understand it.

For instance, the subcontractor flow-down problem has made it difficult, if not impossible, for you to enter into a spare parts purchasing agreement with the Defense Department on the AWAC's planes. Is that correct?

Mr. PINICK. Yes, sir.

Senator LEVIN. Can you tell us how long this has been going on with AWAC's?

Mr. PINICK. I think we have been working on the current ordering agreement for about 2 years, and I might add, I think our people and the Air Force people at Tinker have worked very diligently to try and achieve that.

I think it is also important to note that——

Senator LEVIN. Have you succeeded yet?

Mr. PINICK. No, sir. No, and I am not optimistic. I have discussed that right up to the very top of the Air Force Logistics Command, and I am not optimistic.

Senator LEVIN. What then is the bottom line? The Air Force is not buying spare parts they need for AWAC's, or what?

Mr. PINICK. No. When there is a serious problem, we find a way between us to solve—like what we call an "AOG," an airplane on the ground. That means that we find a way to get——

Senator LEVIN. So if they have got a serious problem, you find ways to get around all the bureaucracy, but if the problem is just a normal problem, an on-going problem, you have not solved it yet?

Mr. PINICK. That is right. The basic blanket ordering agreement, which we are trying to achieve through specific waiver of these clauses that we cannot find a way for our commercial suppliers to accept. We simply cannot seem to get there.

Senator LEVIN. And do the folks at Tinker say that they would love to be able to waive it, but they do not have the discretion, or are they saying that they are glad they cannot waive it, because you are wrong and they are right? What is the general thrust?

Mr. PINICK. No, I think it is the former, Senator. I think they carry those waivers forward, and it seems to die in the bureaucracy somewhere, and some of them, I am not sure it can be waived. Some of the problems are simply unwaivable.

Senator LEVIN. Because of the law, the regulations?

Mr. PINICK. Yes, sir. Some of them simply are statutory.

Senator LEVIN. Did you get any indication from the Department of Defense that they would accept a commerciality provision on LRAACA, by the way, going back to that for a minute?

Mr. PINICK. The answer is no. To the contrary, as it was indicated, we did not win that program, but in a debriefing, we were advised by the Navy that our commercial practices provision was unacceptable.

Senator LEVIN. Identify the two or three biggest sticking points right now on AWAC's. What can they not waive that they would like to waive?

Mr. PINICK. Well, I think it was indicated—it is a big problem with cost and pricing data. There is a provision for waiver, but it is a very difficult one to meet, and I think that is probably one of the biggest sticking points with our commercial vendors, and audit rights is probably the next.

Senator LEVIN. What?

Mr. PINICK. Audit rights.

Senator **Levin**. Okay. Now, if we do not do something to solve this problem, are we likely to run into the same difficulties with other aircraft programs like the Air Force One program or others?

Mr. **Pinick**. Yes. I think this problem is not going to get any better. It is going to get worse. Our view is that in the absence of obtaining these waivers up front—in the contract quite clearly—we simply cannot provide commercial aircraft to a military requirement.

Senator **Levin**. Ms. Williamson, you described problems that you have had with the requirements that must be met to qualify for an exemption to cost or pricing data requirements, and I would like to go through these problems with you.

First, you indicated that the prime contractor on the LRAACA program wanted you to provide cost or pricing data or a standard Form 1412 exemption form, and as I understand it, the prime contract was awarded on a fully competitive fixed price basis and was exempt from those same requirements. Is that true?

Ms. **Williamson**. That is right.

Senator **Levin**. So that even though the prime contractor was not required to provide any of that data to the Government, they were requiring you to provide the data to them.

Ms. **Williamson**. Either that or sign up for a full contract with all of the terms. That is what it finally came down to. They said—Lockheed told us that they were being required to do that by their contracting officer.

Senator **Levin**. So that this was not Lockheed's fault. It was the Government's fault, or how——

Ms. **Williamson**. Yes. Lockheed was trying very hard to work the issue with us, except that in the change of personnel over time—over the 2 years—we had to keep reeducating each new set of people who came onto the program about what the issues were, and the question always arose, "Why can you not provide just a standard Form 1412?" We are buying mostly off-the-shelf equipment, except for seven modified parts.

Senator **Levin**. So that the requirement that you provide this information to Lockheed was not Lockheed's requirement. It was the Government's requirement originally, which they just passed along.

Ms. **Williamson**. According to the letter Lockheed sent us, yes.

Senator **Levin**. And what is the advantage to the Department of Defense to know your cost and pricing data when they have a firm fixed price contract?

Ms. **Williamson**. I cannot think of any advantages. They have gotten the price based on our commercial practices, and they know that through the competition, they have awarded us the contract. I do not know why they would need to look at it.

Senator **Levin**. So you have a situation now where you had competitively obtained a firm fixed priced contract with the prime. And now you as a sub are being required to give cost and pricing data to that prime, which the prime would not ask you for, but the Government is requiring that the prime ask you for it, and you cannot see any advantage—and I must tell you I cannot see any either in a firm fixed priced contract—you do not see any advantage to the Government in gaining that information. Is that a fair summary?

Ms. WILLIAMSON. That is a fair summary. If I could add something?

Senator LEVIN. Sure.

Ms. WILLIAMSON. It seems to me that the Government contracting officers are looking for an easy answer with commercial products. They think "1412" anytime they hear "commercial products." It is a stimulus response. "Commercial products. Oh, 1412." They put it in the file.

They do not do any analysis beyond there, and they want an easy answer, which is why I think a separate button in their Federal procurement system that says, "These are the commercial terms that apply when you have commercial contracts," would make it so that it would be "administratable" from a Defense Department standpoint.

Senator LEVIN. Okay. Now, Mr. Pinick, back to you. As a prime contractor on this type of procurement, can you explain what the reasoning would be as to why a subcontractor would be required to provide the cost and pricing data in a case where the prime was exempted from that same requirement?

Mr. PINICK. I cannot identify any value to the Government for that result, but my recollection is that it is required, but I do not know of any benefit that ultimately flows.

Senator LEVIN. Okay. Ms. Williamson, back to a situation where you might modify an existing part during the program at the Department of Defense request. If you were able to obtain an exemption to sell a part to the DOD to begin with, if you modified a part at the request of the DOD, could you lose that exemption?

Ms. WILLIAMSON. Any Government unique parts cannot quality for the exemption under the standard Form 1412, and it depends on how much the auditor is willing to—well, actually, the contracting officer has the discretion to do it, and they get nervous, so they call in the auditor to say, "Would you accept this if I accepted it?" We have had that happen.

Senator LEVIN. But the question then is: Could you lose the exemption?

Ms. WILLIAMSON. Yes. Yes, distinctly.

Senator LEVIN. So to just summarize what we are talking about here—you have got an exemption to begin with, you modify the part at the request of the Government, and you could lose the exemption as a result?

Ms. WILLIAMSON. Precisely.

Senator LEVIN. Okay. Now, you also have both identified a problem with older products, and as I understand your testimony, the Government would be purchasing a product that could be at or near the end of a commercial production, and as a result, even though your product is commercial now, it might not be by the time that the DOD gets around to buying it. Does that mean you might qualify for an exemption now, but could lose it, because the DOD is slow to complete its purchase?

Ms. WILLIAMSON. It might not be because the DOD was slow to complete. Honeywell supplied the fuel quantity system for the AWAC's aircraft that Mr. Pinick was referring to, and we are one of the subcontractors that got into that trouble where they are still building aircraft, but there is no commercial market anymore for 707 aircraft, and we did lose that exemption and got into the same problem he was in, only with him.

Senator LEVIN. Can you think, either of you, of any specific contract provision which the Department of Defense has eliminated or narrowed in the last 2 years to make it easier for commercial manufacturers to do business with the Government?

Why do we not start with you, Mr. Pinick?

Mr. PINICK. No, I cannot think of anything.

Senator LEVIN. Ms. Williamson.

Ms. WILLIAMSON. I cannot think of any contract terms that have been modified. They have seemingly done a little better on the specification issue.

Senator LEVIN. Do you find that contract provisions are consistently applied, so that you know exactly what provisions to expect in any Government contract?

Mr. PINICK. No, they are not consistently applied.

Senator LEVIN. Ms. Williamson.

Ms. WILLIAMSON. No.

Senator LEVIN. As I understand the process, contracting officers are provided with a list of all possible contract clauses, and then write their contracts by checking off the clauses that they want to apply to a particular contract.

Now without clear guidance as to which clause they should apply to a given contract, I have been told that contracting officers will just frequently err on the side of caution and include too many clauses, which place burdens on contractors to justify the removal of those clauses. Is that the way this thing works? It is just a checklist, and the officer goes through and says, "Include this, include this, include this."

Mr. PINICK. The contracting officer has a very extensive list or recipe of clauses available to him, and yes, he does select those that are applicable according to the criterion in the regulations to the procurement at hand. It is clearly the safe course to put in more rather than less.

Senator LEVIN. And would two different contracting officers reach two very different conclusions as to which clauses might be in the contract?

Mr. PINICK. It certainly could happen.

Senator LEVIN. Would you agree with that, Ms. Williamson?

Ms. WILLIAMSON. I have never seen two alike.

Senator LEVIN. And the difference between putting in 25 clauses, or 50 clauses, or 75 clauses, or 100 clauses is a major difference to the contractor.

Mr. PINICK. Definitely.

Ms. WILLIAMSON. Absolutely.

Senator LEVIN. Do you think that it might be helpful for the DOD to develop a short-form contract, including only those contract clauses that are required in an NDI contract, and require contracting officers to justify the inclusion of any additional clauses beyond that bare requirement?

Ms. WILLIAMSON. I think it is a great idea.

Mr. PINICK. I think that would help.

Senator Levin. Finally, Ms. Williamson, your prepared testimony described a case in which the Air Force wanted four parts for a weather radar system. You indicated that only three of those four parts qualified for the commercial exemption to cost or pricing data requirements. Is it true that the Air Force has gone ahead and bought the three qualified parts?

Ms. Williamson. Yes. They ordered the three for the foreign aircraft buyer, and they still do not have the fourth part today.

Senator Levin. Is there any solution in mind to the fourth part mystery or question?

Ms. Williamson. Well, under the regulations, if the contracting officer wanted to stretch his authority to the maximum, he could just document to the file that he cannot get that part any other way and could accept it without cost or pricing data and without the standard Form 1412.

Senator Levin. And has that happened yet?

Ms. Williamson. No.

Senator Levin. And are those three parts useful without the fourth?

Ms. Williamson. Completely inoperative.

Senator Levin. Anything else?

[No response.]

Senator Levin. We appreciate your coming forward and testifying. It is very helpful.

Ms. Williamson. Thank you.

Senator Levin. It is very discouraging, but very helpful. Thanks.

Finally, we have a panel that consists of John Fluke, Jr., John McGowan, and Al Herman.

Mr. Fluke is the Chairman of the Board and Chief Executive Officer of John Fluke Manufacturing Company.

Mr. McGowan is the Federal Procurements Manager for Hewlitt Packard Company, and Mr. Herman is the General Manager of the Federal Systems Division of Tektronix, Incorporated.

All three witnesses are testifying today on behalf of the commercial product acquisition team or COMPACT, which is an organization created to encourage the Government to place a higher priority on the acquisition of NDIs.

Senator Levin. Mr. Fluke.

TESTIMONY OF JOHN M. FLUKE, JR., CHAIRMAN OF THE BOARD, JOHN FLUKE MANUFACTURING CO., EVERETT, WA[1]

Mr. Fluke. Thank you, Mr. Chairman. Thank you for the opportunity to appear before the Subcommittee.

As mentioned, my name is John Fluke. I am Chairman of the Board of the John Fluke Manufacturing Company.

The Fluke Company manufactures and distributes a wide range of commercial electronic test and measurement instrumentation. Last year, we had sales of about $225 million. About 15 percent was in direct sales to the Federal Government, about 12 percent in sales to Federal Government prime contractors. Obviously, therefore, we view the Government as an important customer.

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[1] See p. 138 for Mr. Fluke's prepared statement.

I might mention, in addition to that, as has been cited by other previous panelists, that the Fluke Company has a group of people about the size of a typical large development program's engineering staff to deal with the Government except these people are not engineering people, they are contracts people. They have a considerable amount of resource for what should be a relatively small fraction of the activity required to administer our government business.

It has been about 3 years since members of COMPACT, myself and others had the opportunity to testify before Congress, and we were pleased to watch the introduction of the Levin legislation which was enacted in 1986. For the first time, I think we had a bellwether piece of legislation that created a statutory preference for the acquisition of commercial products. And thus a major change in the policy landscape in the Department of Defense. That is the good news.

The bad news is nothing much has happened within the Department of Defense in terms of implementing the Levin legislation. There has been no real change in the day-to-day operations of the DOD. So the question is what can be done after both Congress and, indeed, many members of the COMPACT and others interested in the subject have worked diligently with the management inside the Department of Defense to try to effect changes.

First, I think it is very important, as this hearing suggests, to keep the buy commercial notion on the agenda, and we deeply appreciate the members of Congress, particularly yourself, Mr. Chairman, doing this.

Second, we would like to point out that the Commercial Procurement Advocate in the Office of the Secretary of the Department of Defense is a position that does not appear to be functioning. We believe that this position could make a significant difference in the full implementation of the intent of the Levin legislation.

Third, we look at the Federal Acquisition Regulations, and those who write them, and those who have to live under them, the contracting officers. And what we believe we see is not necessarily a situation where more legislation is required, and certainly not a situation where more regulation is required. Quite the opposite. There needs to be a reduction in regulation.

Fourth, we see that the personnel involved in the DOD's procurement process desperately need additional training clearly in commercial contract law, and the adaptation of such law to DOD procurement.

Now, in addition to all the testimony that has been submitted in writing by COMPACT members, I would like to comment on a couple of very specific areas.

First, on the subject of rogue contract clauses. And, second, on the regular demand for cost or pricing data particularly as it relates to the 1412 subject just mentioned before.

We start with the issue of rogue contract clauses and the like. COMPACT recently analyzed seven contracts for the procurement of commercial products. According to our analysis, there were some 170 different standard Federal acquisition regulation clauses that appeared at least once in one of those contracts. There were 53 different standard DOD clauses that appeared at least once in one of those contracts. In addition, there were 34 different standard buying command clauses that appeared at least once in one of those contracts. That is a total of 257 standard clauses.

Not only that, the specifications referenced by many of these clauses invoke other specifications not explicitly stated. And to a supplier like the Fluke Company and thousands of other suppliers that basically are in the commercial products business, such things as the flow down provisions that prime contractors, it seems, must necessarily pass on to us comprise a substantial inhibition to the Government having the fairest and most open competition for the things that it procures. If I could give an example that is cited in the written testimony. It is an example with which I am familiar, although we have generalized the names of the parties involved. And it goes something like this:

A prime contractor wanted to buy two hand-held meters. These are relatively simple items as the name implies. You can hold them in your hand. They are very rugged devices used pervasively by the commercial marketplace. In this case they were to be used as ground support equipment in a very complex system for a particular airplane. The multimeters have a commercial price in hundreds of catalogs around the United States through which the product is sold of $199.

The prime contractor originally telecopied the first two pages of the request for quotation to my company, a commercial vendor, and sent the rest of the request by mail. The rest had to be sent by mail due to the size of the Logistics Statement of Work. Under the solicitation, the commercial vendor for this $199 item would have to commit to:

Ensuring an inspection system in accordance with MIL-I-45208, MIL-C-45662, and/or MIL-Q-9858.

Second, identifying nonrecurring elements of the cost.

Third, supply the product under the DPAS order system.

Fourth, submit cost or pricing data.

Fifth, give the prime contractor access to cost records.

Sixth, mark the items pursuant to MIL-STD-130.

Seventh, agreeing to the special warranty terms as described in the statement of work.

Eighth, following the technical requirements of the statement of work.

Ninth, providing the prime contractor with plant inspection rights.

Tenth, providing written certification that the device has been proof load tested to 200 percent of its rated working capacity. I am not sure how you do that with a multimeter since it is not rated for standing on.

Eleventh, complying with several pages of fine print and contract clauses, some of which add additional military specifications requirements, others that repeat requirements for cost or pricing data, and others that are simply not applicable.

And, lastly, providing supplier test results.

We, the commercial vendor, originally responded to the Prime Contractor in a letter on May 6th of 1987, indicating that we were willing to sell the two items for $378.10. That is about $200 worth of meter, another $178 worth of paperwork I guess is the way you could look at it.

The commercial vendor also suggested that the prime contractor could purchase the parts from an authorized dealer or off the GSA schedule.

In a letter on June 22, 1987, the prime contractor notified the commercial vendor that although the original request for quote was sent based on the assumption that commercial standards would be applicable, further review indicated that all support equipment would have to be purchased to Government standards. The prime contractor then added and deleted various clauses, including additional terms and conditions, which still included technical data rights clauses and various certifications. While that yielded some improvement, the paperwork aspects of the procurement still dramatically exceeded the commercial cost of the products sought.

By letter of June 26, 1987, the prime contractor notified the commercial vendor that, due to the documentation involved, that the due date was to be extended. By letter on July 21, 1987, the commercial vendor again indicated that they would not be responding because it is not cost-effective for the commercial vendor to invest the time and resources necessary to fully implement the requirements.

By letter of July 22, 1987, the prime contractor notified the commercial vendor that the commercial vendor needed to extend its offer through October 30, 1987. The sale was never made.

Now, the good news about this is that it only took most of a year for us to go through this and arrive at the conclusion that we did not want the business.

The bad news is that the Government spent a lot of extra time and money for basically no value.

And I guess the point of all of this is that the Government actually has in the Department of Defense some pretty good people and some pretty good methods for acquiring things that heretofore did not exist. Things that are custom in nature to the specific mission that the DOD has tried to satisfy. And for development items that is just fine.

But what is missing is a much smaller body of regulations, and the necessary training for contracting officers to be able to engage in standard commercial like procurement processes.

This situation is a little bit like each of us when we go and fly some place and perhaps rent a car at the other end of our trip. It would be like having to go through the process of reviewing and signing a lease for commercial retail space, when all we want to do is to rent a car.

It would be like the Fluke Company, for example, in procuring a new building, which is a relatively complicated thing and requires literally hundreds of pages of contracting information.

Using that same approach when we simply wanted to buy a dozen Fleet Cars, which is a much simpler procurement process, it seems that the Department of Defense has only one method of acquiring only one kind of thing, and it is ill-equipped to buy standard commercial products, something we all know.

I think it is inappropriate that we come before Congress only bellyaching. We are also here to try to offer solutions. You might say we are from industry and we are here to help you.

So our suggestion here today, not that there are not many other problems to be addressed, but our suggestion here today is to strongly endorse the notion of the creation of a standard form Government contract for commercial products. COMPACT's review of the FAR suggests it is possible that we can prepare such a contract form and incorporate only 15 to a maximum of perhaps 20 clauses to comply with all the applicable statutes.

The other areas that I would like to comment on, and hopefully they will come out in the question and answer period, such as the Standard Form 1411 and 1412. These are covered in COMPACT's written testimony and will be covered by other panelists here.

In closing, I would like to particularly point to page 26 of COMPACT's written testimony, originally the last page, if your pages are numbered as mine are, that basically summarize COMPACT's current agenda as well as some of the things it is looking to just slightly beyond the implementation of this current agenda.

I appreciate the opportunity to testify before the Committee, and I wish you, as a member of the Board of Directors of the Free World, the best of luck in dealing with this nearly hopeless cause.

Thank you. [Laughter.]

Senator LEVIN. Thank you.

Mr. McGOWAN.

TESTIMONY OF JOHN McGOWAN, FEDERAL SYSTEMS MANAGER, HEWLETT PACKARD CO., CUPERTINO, CA [1]

Mr. McGOWAN. Mr. Chairman, my name is John McGowan. I am the Federal Procurements Manager for Hewlett Packard Company.

Hewlett Packard manufactures and distributes a wide range of products, ranging from electronic test and measurement equipment to computers to health care equipment. Last year, we had total sales of about $10 billion, and of that 4 percent was in direct sales to the Federal Government and about 2 percent additionally was in sales to Government prime contractors.

As Federal Procurements Manager, I am responsible for all our Federal contracts and sales policies, including our GSA contract negotiations, plus functional management for proposal preparation and contracts, as well as training and system support for all the Federal marketing contracts at HP.

I very much appreciate the opportunity to testify this morning. Hewlett Packard and its Chairman, Dave Packard, are particularly interested in trying to improve the Federal acquisition system and to see an improved commercial product acquisition policy implemented.

Like the other COMPACT members, Hewlett Packard shares a concern that much attention has been focused on acquisition problems over the past several years, but little effort has been focused on really taking advantage of commercial products and commercial practices.

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[1] See p. 173 for Mr. McGowan's prepared statement.

Of the many existing impediments that a commercial product vendor wanting to do business with the Government must face, one of the most significant, as indicated in the written statement, is the number of requests for cost of pricing data. Serious problems are encountered in attempting to do business with the Government involving new product offerings or products that have been modified to meet Government needs.

Often, the Government's only solution is to demand cost and pricing data. When a commercial firm like ours is unwilling to do business that way, an impasse results. There has to be meaningful reform of the Government's regulatory policies if these kinds of impediments to the acquisition of commercial products are to be removed. Clearly, unnecessary and inappropriate demands for cost and pricing data represent a significant problem and one that must be resolved. I would like to address two aspects of that problem this morning.

First, we are continually faced with the need to submit a request for exemption from the submission of cost or pricing data, a Standard Form 1412, for products that are currently on General Services Administration Multiple Award Schedule. According to our data, we prepared almost 500 of these 1412 forms last year for products on GSA schedules. More than half of those were for Government prime contractors, meeting the burdens imposed on them by the Government.

What is troubling about all these requests for cost or pricing data, or 1412s, is the fact that Congress has specifically recognized GSA schedules as competitive procedures when it enacted the Competition in Contracting Act in 1984. Despite this competitive status, the Government contracting personnel and prime contractors often require a Standard Form 1412 prior to buying a product listed on the supply schedule.

Although we are sometimes able to eliminate these requests through negotiations, more often than not, the contracting officer or the buyer simply advises us that the 1412 must be provided or no subcontract or contract will be awarded.

As a result, Hewlett-Packard must gather and document all recent commercial sales data for certification of commerciality in each of these Government sales. I should point out that this data is similar and, in many cases, identical to the data that was already provided or certified to when commerciality was established at the time that the GSA schedules were negotiated.

I would also point out that GSA has the rights and does exercise the right to audit this data both prior to award of a schedule contract and after contract completion.

A related problem involves requests for cost or pricing data in solicitations that are competitive. The purpose, of course, of obtaining cost or pricing data is to ensure that the prices paid are reasonable. The current regulations indicate that cost or pricing data should not be required where adequate price competition exists and reasonable prices are therefore obtained.

Despite all this relatively clear regulatory guidance, contracting officers still frequently demand cost or pricing data, even when full and open competition procedures are being utilized. For example, in one recent procurement for computers and communications equipment, over 100 companies attended the pre-solicitation bidders' conference. In a clearly competitive situation, the contracting officer still insisted on cost or pricing data and Standard Form 1412s were required to be submitted in order to remain in the competition.

Even if this particular contacting officer had finally relented and eliminated the cost or pricing data requirement, the process still has a flaw in it. The flaw is the need for companies to negotiate with the contracting officers about regulatory requirements involving cost or pricing data. We estimate that for every two requests under which we do submit the request for exemptions by compiling and submitting the 1412s, we receive at least a third such request which is ultimately eliminated through negotiation. This is costly for us and still requires us to maintain a full-time staff to prepare and support the audits of all these certifications.

On a hopeful note, DOD has in fact amended the DFAR effective the 31st of May, to incorporate in a 2-year old policy letter that discourages but still does not eliminate cost or pricing data requests for competitive procurements at the prime level.

Unfortunately, since this new guidance is still somewhat internally contradictory, relief still may be out of our reach.

One additional area of concern is the manner in which the Government evaluates the lowest total overall cost of any particular commercial product. The concept of lowest overall cost is the maxim of the law, and is in fact not inconsistent with buying decisions in the commercial market. In the commercial marketplace, buyers evaluate products not only on the initial product price, but also on the basis of long-term quality cost factors such as reliability and maintainability, as well as vendor performance. However, Government contracting officers have become far more comfortable evaluating commercial products on the single factor most easily quantifiable, which is the initial or instant product price. Even when quality cost factors are officially included in procurements, they are often treated in a pass/fail fashion, with the final decision based on lowest price.

Recognizing that it is not always in the best interest of the Government to make acquisition decisions based entirely on initial price, a few buying commands have instituted experimental or trial programs. We would like to commend the program operated at the Army Communications Electronics Command at Fort Monmouth, called the Blue Ribbon Contract program. The Army is attempting to objectively evaluate contractors based on past product quality and delivery performance. The program would permit a contracting officer to award a contract to a certified Blue Ribbon contractor as long as their product price is within 10 percent of another bidder's offered price. An even higher differential may be permitted if approved by the Director or Deputy Director of Procurement.

This effort is an excellent start at trying to recognize and evaluate the genuine costs associated with the life cycle of any particular product. Such efforts need to be encouraged at the buying offices throughout the Government.

The Air Force, in the last several months, has recently initiated a program they refer to as "Competition for Performance" where they are also attempting to recognize factors other than just low bid.

In addition, the lessons learned from these programs need to be collected and evaluated so that program and evaluation process can be improved.

Let me conclude by restating again we appreciate your attention to these issues. These issues may never be as exciting to the public as performance problems in some multi-billion dollar weapons system, but at the same time, the solution to these problems will go a long way towards achieving the full benefits of competition in Government contracting by ensuring that the real additional costs of doing business with the Government are kept to a minimum, and the impediments are removed.

Progress here can bring more commercial suppliers back into the competitive process.

And I would be pleased to answer any questions you may have.

Senator Levin. Thanks so much, Mr. McGowan.

Mr. Herman.

TESTIMONY OF AL HERMAN, GENERAL MANAGER, FEDERAL SYSTEMS DIVISION, TEKTRONIX, INC., BEAVERTON, OR[1]

Mr. Herman. Mr. Chairman and Senator Cohen, my name is Al Herman. I am General Manager of the Federal Systems Division of Tektronix, Incorporated, located near Portland, Oregon.

Tektronix is an electronics manufacturer of commercial off-the-shelf design, test, graphics and communications products. Last year, Tektronix's consolidated sales were slightly over $1.4 billion. Our direct sales to the U.S. Government were approximately 9 percent of the consolidated sales, or about $125 million.

And I also would like to begin by thanking you for the opportunity to testify here today.

You have already heard quite a bit about the cost and pricing data problems, but I would like to continue with them because it is our current primary concern. Like most other commercial vendors, Tektronix relies on a commercial accounting system which is designed and scaled to meet our commercial needs. Our systems are the absolute minimum size and scope necessary to ensure that our businesses can be conducted responsibly and that appropriate reports can be provided to managers, shareholders and so forth.

Commercial vendors like Tektronix simply cannot afford to develop and maintain the elaborate cost accounting systems that are required of cost-based Government contractors. Our ability to compete successfully in the intensely competitive commercial electronic marketplace depends upon our ability to operate at costs comparable to those of our international competitors.

Commercial vendors, such as Tektronix, necessarily rely upon a market driven catalog pricing system. Our prices are based on a number of factors, but to a great extent they are driven by the supply and demand fundamentals which are the basis of our successful national economic system. In other words, the marketplace determines their fairness and reasonability.

Despite our commercial pricing program, under the current cost and pricing regulations, and perhaps even more importantly, under the increasingly stringent interpretations of individual contracting officers, we often receive requests for cost and pricing data on acquisitions of commercial products where the Government is clearly protected from unreasonable pricing.

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[1] See p. 180 for Mr. Herman's prepared statement.

I would like to relate an example to illustrate how involved the problems can be that these seemingly simple requests create.

Tektronix recently responded to two solicitations for specialized cable test products. Those particular solicitations required the submittal of sample instruments so the agency could test them and ensure their needs would clearly be met. Vendors whose products passed the test would then be solicited on a competitive basis. The products Tektronix submitted were current catalog items, but were soon to be replaced commercially by upgraded versions.

Although the upgraded products were not yet being shipped to the commercial public, they were nevertheless offered to the agency who tested and agreed to accept them. And I might add that the changes in the upgraded versions had to do with improvements in reliability and maintainability and replacement of the CRT with a flat panel. Functionally, they were very similar.

As it turned out, no other vendor's product passed the test requirements of either solicitation. Because there was no competing vendor, the solicitation was converted from a competitive sealed bid to a single source negotiated RFP requiring cost or pricing data.

Since the products were commercial, and we could not provide the cost or pricing data—we did not have it—we requested an exemption. In order to show substantial sales to the general public of the new products, Tektronix had to convince the contracting agency to accept sales data based on sales of the earlier submitted versions of the items being offered. This is because the agencies would be the first substantial purchasers of the upgraded items, because the introduction into the commercial marketplace was not scheduled until late 1987.

Tektronix during this period also had to convince the Government to recognize that a recent large Government buy of one of the prior products had skewed the percentages of sales to the extent that it now fell into the gray area for qualifying for an exemption from cost or pricing data submission.

However, by examining 2 years worth of data, then by comparing the sales data of the similar products, it was clear that the products were in fact sold at catalog prices in substantial numbers to the general public. And the Government finally accepted the sales data. However, we were not home yet.

By the time all issues were finally resolved with regard to pricing of the spares and the technical data, the upgraded versions were in commercial production. The Government then advised Tektronix that the originally submitted request for exemption had expired and new claims for exemption were required. Revised sales data, based on sales of the new models were submitted twice.

The first revision included sales covering the first 3 months of commercial production. The quantities sold during the first 3 months were deemed too low by the administrative agency to grant the exemption.

Nearly 4 months later, a second revision, based on 7 months of commercial sales, was submitted. By this time, Tektronix was able to demonstrate substantial sales to the general public by virtue of the fact that it was shipping the product to everyone but the contracting agency who needed them.

The Government finally accepted the sales data and granted the exemption 1½ years later. To give you an idea of the amount of effort that went into this process, I have beside me here a portion of the paperwork which I am told is approximately half of the paperwork that was involved.

Senator LEVIN. It is almost as thick as our Continuing Resolution last year. Up until then, I think it set the record for weight. [Laughter.]

Mr. HERMAN. Someone read our documents. No one reads the Congressional one. [Laughter.]

I would like to enter this in the record.

Senator LEVIN. It will not be made part of the record. A photograph of it will be made part of the record. [Laughter.]

Mr. HERMAN. A similar sale to a commercial customer would have taken a few pages of documentation.

A related problem occurs when the Government wants to buy spare parts for commercial products. To facilitate their need to service their own equipment, some agencies buy spare parts for electronic equipment at the assembly level rather than the component level. This simple change creates a significant administrative problem for a commercial vendor. Spare parts for commercial products are often available only from the manufacturer and almost always at established and published catalog prices.

However, some parts, particularly the assemblies mentioned above, are purchased almost exclusively by the Government. Therefore, we often do not have commercial sales to meet strictly enforce regulatory tests for receiving exemption from cost and pricing data.

Again, considerable time, measured in months and years, is spent negotiating with the Government for a way around this roadblock. Even though there is no question regarding the commerciality of the products for which the spares are being purchased, or the fairness of the price for the spare parts. One agency has even decided to buy extra complete products which we will ship, unassembled, for their parts.

Procuring agencies, therefore, are caught in these regulations, just as the contractors are. But most contracting officers are reluctant to stick their necks out and seek innovative solutions to the current procurement problems.

I want to emphasize that seldom, if ever, is there a discussion about whether the prices being offered by off-the-shelf vendors is reasonable or unreasonable. The discussions, negotiations, correspondence and paperwork focus almost exclusively on interpretation and satisfaction of the current regulations applicable to granting exemptions from the submission of cost and pricing data. Paperwork, not price, is the issue.

I would like to point out also that disclosing proprietary cost data is not, in itself, the problem. It is the requirement to certify the accuracy of the data based on the Government's cost accounting standards.

For commercial companies to implement and operate Government-approved accounting systems for the small amount of dollars that the Government sales represent, relative to our commercial sales, would be unreasonably costly. It would significantly impact our prices and put us at an even greater pricing disadvantage to our foreign competition, and would not provide any benefit to anyone.

Another impediment for commercial vendors doing business with the Government is the current requirement for source inspection. Successful commercial companies have strong commitments to meeting the quality requirements of their commercial customers, both domestic and international. Companies failing to satisfy customers do not survive in the long run.

The quality control process and documentation requirements of the Government are largely redundant with our commercial quality control process. Moreover, we believe that marginal or no added benefit is achieved as a result of the Government inspection process.

We have no doubt that the process is justified for firms involved in the manufacture of critical, noncommercial, low volume products and firms with little or no experience in the product field for which they have a contract. In contrast, we believe the Government should rely on an established commercial company's quality control system for non-critical commercial products, unless a significant problem arises.

Government source inspection should be limited to products involved in mission-critical situations. If a problem does arise, then the commercial vendor could be subject to source inspection unless it demonstrates that its quality systems are effective.

The Government should also avail itself more of another protection that has proven its effectiveness in the commercial marketplace—that is, the commercial product warranty. Although one occasionally sees reference to greater use of commercial warranties by the Government, from our standpoint, relatively little use of them seems to be occurring.

Although warranty work does increase the manufacturer's cost for the product, it has several benefits. It provides the manufacturer with critical information about product failure so that improvement can be made. It permits repairs to be made properly and more quickly with the right equipment and trained technicians, thereby reducing the number of products being returned to the user with improper parts. The user only knows that his Tektronix product is not working right.

It provides the commercial vendor with an opportunity to market its maintenance services which often provide a more cost-effective way for customers to maintain their equipment, increasing their satisfaction. Tektronix has 46 sales and service offices throughout the United States. Our Detroit facility, for example, has some 50 sales and service employees.

The last impediment I would like to talk about today is the improper use of the Defense Priorities and Allocations System known as DPAS. As you may know, Section 2071 of Title 50 of the U.S. Code authorizes the President to require expedited performance under contracts when deemed appropriate to promote the national defense.

However, lack of clear regulatory guidance permits virtually unrestricted use of the DPAS rating system. Most of the DOD and many of the DOE orders which we get are DPAS rated. We recognize that national defense is a high priority.

However, unnecessary and unlimited use of the DPAS ratings requires us to develop special and costly order processing procedures, establish special buying requirements, shift production schedules, and delay delivery to commercial customers. This is particularly troublesome when a priority rating is used in cases where the product is destined for storage in a Government warehouse.

Mr. Chairman, this concludes my remarks. I apologize if they seem negative, but I am focusing on the problems in the system. On the positive side, there are many dedicated people in the procurement system who faithfully and conscientiously strive, on a daily basis, to make it work in spite of the problems with the regulations. And I am encouraged that your Committee is looking into these problems.

I will be pleased to answer any questions you may have.

Senator **Levin**. Mr. Herman, we thank you and all the other members of this panel for your very candid, although very discouraging, testimony.

First, Mr. Fluke, in your prepared testimony, you noted that COMPACT prepared an August 1987 report for the Department of Defense, in which you identified 35 specific regulatory and procedural impediments to the acquisition of NDI's.

What is the status of those 35 impediments? Have any of them been removed as a result of the legislation which you referred to, which we adopted about 3 years ago?

Mr. **Fluke**. To the best of my knowledge, Mr. Chairman, virtually all of those regulations still are operative to one degree or another, way beyond the extent to which they should be in connection with NDI.

Senator **Levin**. Can you think of any specific example of a contract requirement or clause that the DOD has eliminated as a result of the NDI provision in the law of a few years back?

Mr. **Fluke**. On my own behalf, nothing leaps to my mind. Perhaps the other two panel members might know.

Senator **Levin**. Can either of the panelists answer?

Mr. **Herman**. No, sir.

Mr. **McGowan**. Again, some moderate relief in specifications, but nothing in terms and conditions.

Senator **Levin**. All right. So, despite the intent of that law of a few years back that we passed, you have not seen any significant impact yet?

Mr. **Fluke**. No, sir.

Senator **Levin**. Now, Mr. Fluke, you testified about a case in which a prime contractor sent you a 2-inch thick solicitation for a couple of simple testing devices that your catalog priced, I think you said, at $199 each.

Mr. **Fluke**. Yes, sir.

Senator **Levin**. So, this was a solicitation for a $400 sale?

Mr. **Fluke**. Yes.

Senator Levin. Is that right?

Mr. Fluke. Yes.

Senator Levin. One of the ways around this would be to have a short-form, which—I think you have indicated you would support a short form contract for NDI items?

Mr. Fluke. Yes, sir.

Senator Levin. You testified that you thought that we could reduce the number of clauses in that short-form contract to perhaps 25 clauses.

Mr. Fluke. Or less, yes.

Senator Levin. Or less. And that currently, a contract could have 200 to 300 clauses?

Mr. Fluke. That is correct.

Senator Levin. Do you believe that a short-form contract could be created without any statutory change? Do we have to mandate it or could the DOD just go ahead and do it?

Mr. Fluke. It is clearly theoretically possible for the DOD to proceed to do this. It has been possible, and under the intent of the Levin legislation, it appears to me that there is a pretty clear legislative mandate to proceed with such activity.

As a practical matter, what it might take to cause these changes is a more difficult problem to deal with and a much more difficult problem, therefore, to answer. I suppose one answer to the question is, instead of attempting a direct legislative assault on the problem, is to go back and look at how one might manipulate the purse strings attached to the DOD purse to encourage cooperation in this respect.

Senator Levin. Okay. Mr. McGowan, you have given us a classic example of what appears to be bureaucratic overkill, and that is the GSA example.

As I understand it, you provide basic data and a certification to the GSA, get approval for commercial sales to the Government—so you have got GSA approval over here. Then another agency, the DOD requires you provide them with the same data, the same certification before you can sell it to them; is that correct?

Mr. McGowan. That is correct.

Senator Levin. Okay. So, first let us go through that process.

Is the information that you provide to the GSA and to the DOD, essentially the same information?

Mr. McGowan. It is essentially the same information. We are certifying and providing supporting data in both cases that we meet the exact same regulation in the Federal Acquisition Regulation, the basic requirement for commercial price exemption.

Senator Levin. And the GSA then audits that data before it includes your contract on their price schedules?

Mr. McGowan. Yes, they do.

Senator Levin. And you have given both agencies the same certification, that you are giving them your best price?

Mr. McGowan. We are certifying as to the commerciality of all of the products involved, and we are also certifying that the prices qualify for the commercial price exemption.

Senator Levin. And the GSA makes the determination that that is correct, in the first instance?

Mr. McGowan. Yes, they do.

Senator **LEVIN**. Then the DOD makes the exact same certification?

Mr. **McGOWAN**. Yes. It is both the DOD and the prime contractors, but they both go through that same process.

Senator **LEVIN**. Now, if the DOD were purchasing a substantially larger quantity and thought it should get a price break, would it still be possible for the DOD to accept GSA's determination of commerciality and try to negotiate a lower price for itself?

Mr. **McGOWAN**. It is possible. In some cases, it is, in fact, achievable in some of their multiyear, major procurements. But the GSA contracts that are negotiated are negotiated based on the aggregate dollar volume of the GSA purchases to begin with. So, if we assemble all the Government purchases that are expected under the schedule, then that becomes the basis for the dollar volume or the discounts of those contracts.

Senator **LEVIN**. As I understand it—I think, Mr. Herman, you can perhaps best answer this question—there are some instances in which the DOD has been unable to purchase a needed part because of regulatory requirements. Instead, the DOD purchased a complete instrument, asked for it unassembled, took the parts that it needed, but that it could not purchase because of the regulatory requirement, used the part it needed, and threw away all the other parts.

Is that really true?

Mr. **HERMAN**. The story is basically true, but I do not want to mislead you as to what really happened. I know that you took that from our submitted statements.

Senator **COHEN**. Could you pull that mike a little bit closer?

Mr. **HERMAN**. Yes.

Senator **COHEN**. We do not want to miss any of the details on this. [Laughter.]

Mr. **HERMAN**. The issue of this case, let me repeat, was not the fairness of the price. The DOD buyers were able to determine, just as a commercial buyer might, what the boards were worth, based on an analysis——

Senator **LEVIN**. What the what?

Mr. **HERMAN**. It involved some circuit boards. I am sorry.

Senator **LEVIN**. What the circuit boards were worth?

Mr. **HERMAN**. In an electronic device.

They could look at the complexity of the board, the number of components, the number of layers and so forth, and compare it to other boards. So, we had established, very early in the process, that it was priced about where it should be. If it was not, Tektronix would have reduced the price just to sell the things because they were causing a procurement problem.

I cannot state that this procurement approach resulted in an increased cost to the Government. There were a number—I believe all—of the circuit boards in the device could be used as spare parts. What probably came out of this was, there would have been some knobs and the case and some other things that the Government could not have used.

The real significance of the example, in my mind, is that it shows the contractual gymnastics that the contracting officers, who are committed to equipping the forces in spite of the regulations, that they have to go through. And anyone who understands the business and who would be candid with you will tell you that there are a number of others.

In some cases, they will redefine their procurement philosophy. In some cases, they will procure at the parts rather than the assembly level. In some cases, they will redefine the quantities they need so that they miss thresholds. This is the reality of the thing.

Senator Levin. Sometimes they reduce the buy significantly into pieces and buy four or five——

Mr. Herman. They might do that also.

Senator Levin [continuing]. Contracts instead of—dividing it into four or five—let us go through these gymnastics before we lose that, just on the circuit boards, if I can.

The DOD needed a circuit board for that particular item; is that correct?

Mr. Herman. Senator, it needed several circuit boards.

Senator Levin. It needed several circuit boards.

Were all the boards part of one item?

Mr. Herman. Yes, sir.

Senator Levin. And what was the item called?

Mr. Herman. It was a spectrum analyzer, if I am not mistaken.

Senator Levin. What generically would it be? A measuring device?

Mr. Herman. It is a device that converts frequency data into time domain data. It looks at frequencies emissions, picks out individual frequencies and displays them.

Senator Levin. It needed some circuits boards for this device.

Did it try to buy those circuit boards as spare parts?

Mr. Herman. Yes, sir.

Senator Levin. And it could not buy them separately?

Mr. Herman. It tried to buy them from us.

Let me mention that Tektronix is not in the spare part business. We do not OEM any spares. We supply people who buy our products with spare parts for our products. If we procure those spare parts, we recommend to our customers that they go directly to the vendor if they want to do that. We give them the part number that our vendors use.

Senator Levin. But did they try to buy the circuit boards by themselves?

Mr. Herman. Yes, sir.

Senator Levin. From whom?

Mr. Herman. From us.

Senator Levin. And would you sell them to them?

Mr. Herman. Yes, sir, but they then indicated that they would have to have cost and pricing data for the spares.

Senator Levin. And did you tell them that you could not give them the cost or pricing data for that?

Mr. Herman. Yes, we could not do it. We did not mind telling them what the parts cost us, but when you provide cost and pricing data, you have to certify it. We all know what happens if you make a mistake in that process.

Senator Levin. So you could not sell them the circuit boards under the conditions that they set down; is that correct?

Mr. Herman. That is correct.

Senator **Levin**. Because you would have to certify to certain cost or pricing data. And the way around that, the mental gymnastic around that then was for them to buy the entire device?

Mr. **Herman**. Yes, sir.

Senator **Levin**. Unassembled?

Mr. **Herman**. We packaged up the parts in envelopes, and sent it to them as a kit.

Senator **Levin**. So it would be unassembled in a kit and they could just pick and choose the parts they needed?

Mr. **Herman**. Yes, sir.

Senator **Levin**. And throw away the balance?

Mr. **Herman**. I do not know what they did with the balance.

Senator **Levin**. But they did not indicate any need for the balance, as far as you know?

Mr. **Herman**. No, sir.

Senator **Levin**. Now, what you are saying is that—did that kit cost them more than the circuit boards would have cost them?

Mr. **Herman**. I do not believe, in this case, it did, Mr. Chairman.

Senator **Levin**. And that is what you were saying before, that even you cannot say that it ended up costing them more, the gymnastics that they had to go through in order to get what they really wanted is what the point is in that story?

Mr. **Herman**. Yes, sir. That is the point. It is nonsense to have to go through this just to supply the fleet or the troops with equipment.

Senator **Levin**. And why is it you could submit the kit without certifying as to cost or pricing data, but not submit the pieces of the kit?

Mr. **Herman**. Well, the kit was a complete product, but it was shipped in an unassembled form, and as a complete product, we had the required commercial sales history to support the fact that it was a commercial product.

Senator **Levin**. Gymnastics 103.

Senator Cohen.

Senator **Cohen**. You say, Mr. Herman, that cost was not a factor in your mind.

How do we deal with the situation in which the Government, the DOD, comes to a contractor and says, "I need that circuit board"? That contractor would love to sell it to the DOD but he will not give a certification. He does not want to run the risk that a mistake is involved because it will come back against him.

How do we compare that particular situation against a contractor who simply wants to sell them the complete circuit board kit for a higher price?

Let us suppose that everybody in the business does not want to certify anything. They do not like the certification process, and if certification is insisted upon they do not want to do business with the DOD. The Department of Defense must have the equipment, so DOD buys the entire thing.

Does this situation lend itself to unscrupulous small businessmen arriving at a higher price for a product, where if they had certified the lower cost item, it would have benefited the taxpayer?

Mr. **Herman**. If I understand your question, the whole idea of the regulations regarding spare parts procurement, I think, is to prevent contractors from gouging the Government for the spare parts once they know they have to have them.

The simple way for the Government to establish that the commercial price is a fair one is to look at it commercially—that is, the commercial value I should say.

An unscrupulous contractor could, in any case, just say, take it or leave it. You have got the products, you need the parts, you will pay what I ask for them or you will not get them. Cost data doesn't prevent this.

Mr. McGowan. If I could comment on this.

We have an analogous situation where the products have a well-established sales history, but because the commercial customers typically call us for repair or replacement and get the repair products built into the service charge, we do not have the same kinds of sales history for the spare parts.

But the commercial catalog for the base product is established.

Senator Cohen. Mr. Herman, what about a new contractor coming into competition who does not have that kind of sales record, but has a new circuit board that he thinks he can produce for a lower price than Mr. Fluke. What does he do with it at that point? Does he say, "check my record" or "I am willing to certify them?"

Mr. McGowan. Well, the distinction is that the circuit boards and the spare parts are, in fact, sold at a catalog price, and while we may not be able to achieve the same volumes to meet all the requirements, the certification, the pricing for those spare boards is, in fact, a catalog price, rather than——

Senator Cohen. But what if somebody comes in and says, "I can beat the catalog price and I want to do business with DOD, and I am going to undercut what is in the catalog?" At that particular point we are putting pressure on the Department of Defense to achieve the lowest possible cost.

Can DOD go to that contractor and insist upon a certification of the price?

Mr. McGowan. If you, in fact, have competition between two or three or as many potential vendors who want to supply that part, then the certification requirement disappears altogether.

Mr. Fluke. I think the problem here is, in this case, it is not possible for another contractor to step forward, reasonably speaking, and supply these particular circuit cards.

These are unique Tektronix designs in this example, that Tektronix, rightfully so, should and would refuse to reveal the necessary detail to allow anybody else to make these circuit cards, because they contain propriety information pertinent to Tektronix commercial market for this product.

Senator Cohen. Explain something to me. If a product is unique, then how is its commerciality established?

Mr. Fluke. This is, I think, a crucial point to the general concept of why it is the DOD legislation and just do it like it should, because it is obvious to me that it should.

The DOD does have some peculiar requirements. I was aboard the battleship *Iowa* here in January before the tragedy on it, talking, as a matter of fact, to some of the users of both Fluke and Tektronix and Hewlett-Packard equipment.

That ship, when it goes on the battle line in the Persian Gulf, for example, or in the Mediterranean or someplace, it has to be prepared to be the last ship standing in its particular fleet. Therefore, it has to have a level of self-sufficiency that is not found, necessarily, exactly, in the commercial world.

On the other hand, if you take say a fish processing vessel up in the Gulf of Alaska that has to be on station and operating for the time the fish are coming in, and operating fully, they have a somewhat similar self-sufficiency requirement.

The way these two parties would approach this challenge, I think, is the essence of what needs to be done here. The DOD goes and jumps through all these paperwork hoops and forgets what it was trying to accomplish.

The fish processing vessel owner would simply come to the companies that it is dealing with and say, look, I need certain kinds of spares that may be different than you would normally supply, because I am in the Gulf of Alaska. I cannot get my equipment off of this ship into one of your service centers. It simply is not practical. I have to move the whole ship back.

So, let us sit down and negotiate an arrangement whereby I can keep all this stuff running. Maybe it is a Catapillar tractor and we supplied a generator set aboard the ship, for example. A commercial customer and a commercial supplier can sit down and in 5 or 6 pages or 10 pages or something, define a set of spares, define reasonable pricing, and accomplish a procurement under conventional, commercial contract law.

The DOD has no such facilities. They cannot think this way. In fact, in this Tektronix example, had cost and pricing data been supplied, what would have happened is, these circuit cards would have been enormously expensive because Tektronix does not normally build them in their commercial practice, and could have justified, had it been willing to dump its place upside down for this small order, probably could have justified a price about five or six times its cost because of all the overhead involved in preparing these spare parts kits.

The point is, the DOD has no tools. Its people are not trained. It has no equivalent of the Universal Commercial Code, by which to do commercial acquisition. And it needs those two things and it needs them desperately. Until it gets them, nothing is going to change.

Senator COHEN. Are you suggesting also, that at the commercial level, the owner of that ship would have just wanted a warranty for the parts and not bothered with certification of cost data?

Mr. FLUKE. I think what would have happened is, if a failure happens within the warranty period, then the warranty specifies that no cost will be incurred by the owner of the product in the process of the supplier repairing it.

There may be stipulations in there as to where the repairs can be conducted, but it is not unusual for companies making equipment that is going to go to remote locations to amend their warranty, again through a negotiation under the Universal Commercial Code, that ends up providing a special contract and will, in turn, assure that customer that he can get his equipment serviced in that remote site in a fashion that is satisfactory to him.

It may involve the air freighting of parts and helicopter delivery or whatever. But all those things are routinely negotiated, literally millions of times a year by commercial customers dealing with their commercial suppliers. And the DOD spends a whole bunch of money and usually comes up with unsatisfactory answers in its attempt to accomplish this same purpose.

Senator COHEN. Mr. McGowan, you indicated that you had a product that was certified with the GSA?

Mr. McGOWAN. Correct.

Senator COHEN. And then you had to duplicate the same process going to the DOD?

Mr. McGOWAN. Yes.

Senator COHEN. Are you suggesting that we have a system where if one product, which is not a specialty item or some unique defense requirement, has been certified by one agency in the Government, and that agency has made an analysis of the cost data, then that certification should be sufficient for any other agency?

Mr. McGOWAN. It certainly ought to be, under comparable procurement situations. I would like to comment also, that the industry has had concerns over GSA's——

Senator COHEN. Well, they were comparable in your situation. You had to do the same thing twice.

Mr. McGOWAN. In fact, we do multiple certifications for the same product to the same agency in a 12-month period.

Senator COHEN. It is almost a reverse of the debarment situation that the Chairman and I have been dealing with since we came to the Senate together. When we first started looking into some of these matters, we would find that a particular contractor might be suspended or debarred from doing business with one agency, could then walk across the street and do business with another agency. The debarment would not apply to any other agency.

Senator Levin and myself have been trying to establish a uniform debarment process such that one contractor who commits a fraud upon the Federal Government ought not to be going into a different agency and doing the same thing all over again. This seems to be the reverse situation, where even though you have a certification for one agency, it is not good enough other agencies, and maybe that is something we really ought to focus on.

But I want to just broaden it a bit. We talk about DOD, and I think we are in a habit of picking on the Defense Department because they have such a big budget and they are somewhat intractable to deal with from time to time, to which we certainly can attest. We talked about the $2 box for a 5 cent O-ring, and the 1-inch thick solicitation for a $200 item, and these have to be of some concern to the Department of Defense to have this kind of display take place.

I gather that it is not unique to the Department of Defense. I am told, for example, that GSA buys only phone tool kits to fix the phones that will pull vacuum tubes out of the phones. But we have not had vacuum tubes in phones for I do not know for how many years, and yet that is all that GSA will do.

So, it seems to me that this problems may not be unique to DOD, although I would solicit your opinion on this. Is it something that is Government-wide? Is it more aggravated, perhaps, in DOD than the other agencies?

Mr. McGowan. It is definitely Government-wide. I am not familiar with the telephone tool example—we are not in that business—but I can certainly cite examples of the requirements for data from GSA. We maintain a fairly large headquarters' staff that does nothing but put proposals and support the data collection, the audit requirements. We maintain a private audit conference room for the auditors' use when they come calling on us. There are stories of boxes in the halls at GSA filled with contractor proposals, so there are some requirements for data and paper at GSA—and it applies to the other civilian agencies as well. They just do not get quite the publicity because their individual budgets and examples are not quite as colorful.

Senator Cohen. Could you give me—perhaps the three of you—give me some reaction to this issue where a prime contractor requires the submission of cost and pricing data to the subcontractors when, in fact, the prime contractor does not have to provide that to the Government? What is your reaction to that? Should that be a policy, whenever the prime does not have to submit that information because it is out to competitive bid, then the subcontractor should not?

Mr. McGowan. You need to look at a very specific set of examples, and the example of a fixed price contract at the prime level that was awarded on the basis of competition. At that point, the requirement for certifications and cost and pricing data at the lower tier subcontractors, especially after award of the prime contract, really benefits nobody.

In those cases, at the regulatory level and—at the DOD, there are even people on the staff who would argue that it might not be required. But for a prime contractor to maintain peace with the local contracting officer and administrators and their local auditors, they may have an approved purchasing or subcontracting system that says they will get that data anyway.

And so, the system prevails across the board at the prime contractors. And in some cases, they are forced, by the contracting officers—and in some cases, they do it just because it is part of the system they have already sold to the Government.

Senator Cohen. The Chairman advises me that the question has been explored before, so let me just move on to a final question. It concerns the inspections that are currently being conducted by the Federal Government, in addition to those of the commercial vendors.

This Subcommittee has been inquiring into various areas—medical lab testing, biological weapons research labs, and the inspection of meat and poultry by the Federal Government. In each of these cases, we have found a situation of inadequate training of the Federal inspectors and of major flaws in the inspection process, either because the inspections are too infrequent or perhaps not rigorous enough, depending upon what the situation is.

But you seem to suggest the opposite, that the Government inspections of commercial products are redundant, and that the commercial industry's own quality assurance should be sufficient.

We have had report after report of contractor fraud in various spare parts that do not work, of overcharging, and so forth. How do we deal with this situation? We, as a policy now, rely upon the individual contractors to provide the inspection work? Is it simply a case of warranty and that should be sufficient? Should there be no Federal oversight, no Federal role in the inspection process? What do you recommend?

Mr. **Fluke**. I think the most important opening statement to the answer to, I think, a very important question is again the issue of—are you talking about nondevelopment items or development items? If you are talking about something that has heretofore has never existed, a new torpedo or a new missile or something of that sort, there is quite a different array of pre-shipment certifications that need to go on, as well as ongoing inspections during the first few dozen or 100 deliveries of whatever it is.

If you are talking about a standard commercial product, there is a whole set of different practices that ought to be in place. It is not unusual for dealings between commercial suppliers and their customers to have, essentially, inspections accomplished by the customer of the supplier's production processes, documentation, and the like.

That is essentially a vendor certification process. It is a well-documented approach that is, nonetheless, done uniquely by different commercial customers when they go and inspect their commercial supplier's facilities.

Having once done that, that is sort of the end of it. What these days is the current style, and particularly in Japan and some of the other tigers in Asia, is having once certified their suppliers, they essentially not only cease inspection of the supplier's facilities, but they cease incoming inspection of the product being delivered by the supplier.

If a problem occurs, then, of course, the punishment is very harsh. In some cases we have dealt with, with some of our commercial customers who have told us that once they find that our component that we are selling to them is the cause of a problem in the product they in turn are selling to their customers, that they will give us one chance to fix it and if we do not fix it, then they will find a different supplier.

And conversely, if we do not ship them a bad product, they are never going to bother us. So I guess what I am saying is, it takes a highly knowledgeable, well-trained staff of people in a commercial customer to go back and originally certify a supplier, and then a set of rationale procedures to deal with any faults in the system should they occur.

In the case of Government inspection, it is all done by rules. It is as though we have tried to create a body of rules so as to not have to, any longer, rely on human judgment. And unfortunately, there is no possibility of creating a body of rules thorough enough to deal with the breadth of things that the DOD must procure.

We need the very best people we can lay our hands on in our DOD procurement process, well-trained, and having a high degree of expertise in each of the areas of material procurement that go on. Again, until we get to that training process and get a motivation system in place that makes it work—you have to realize that all three of us, I think, obliquely at least, criticize contracting officers for failing to take the risk in dealing with the commercial product acquisition area that they should take, that is reasonable to take.

You have to understand that maybe the reason why they do that is if they take the risk and succeed, there is no reward. If they take the risk and fail, there is only punishment. And so perhaps motivation is clearly backward in this situation, as well as the absence of training and a careful alignment of an individual's expertise with the area in which he is going to be involved in making procurement judgments.

We basically need to return to utilizing that unique quality that only human beings can bring to a process, and that is this idea of enlightened judgment. Until we get back to that, and so long as we continue to rely on rules alone, the situation is not going to get any better.

Senator COHEN. Thank you, Mr. Chairman.

Senator LEVIN. I do not think we should leave on a discouraging note that way. Let us go back to the warranty issue.

If the DOD made greater use of warranties, would we be able to avoid some of that excessive rulemaking that guides these inspections?

Mr. FLUKE. Absolutely,

Senator LEVIN. Then why do they not?

Mr. FLUKE. Well again, in the case of nondevelopment items, there is not the body of—a much smaller body, by the way—of regulation configured to allow the contracting officers to take advantage of warranties. It just is not in the cards.

Senator LEVIN. What is there that is missing? Is it something that tilts against warranties or is it just pure inertia?

Mr. FLUKE. Well, I think it is—and the other two panelists might want to comment on this—but I think it is the fact that the regulations simply do not recognize the possibility of a supplier coming to its customer and saying, customer, I commit to supplying you this product in good working order that will meet or exceed its specifications, and it will do so for some period of time—90 days, 1 year, or 3 years, whatever the warranty might be.

The system cannot recognize that and accept it as a feature of the product. There is a whole body of regulation that——

Senator LEVIN. Why does this system not recognize it in a Government purchase, but a private system does recognize it?

Mr. McGOWAN. Maybe I can answer that.

One of the elements in the standard Federal contract law is the concept of final inspection and acceptance and payment occurring at the moment of transfer of title, and it is very difficult for the contracting officers to build into those kinds of contracts a continuing obligation on the part of the contractor to remedy a problem 6 months or 1 year after final inspection and acceptance and delivery.

There are also some problems with the application of the warranty if the equipment that was purchased here is on board a ship. It may be difficult to get it back and take advantage of the warranty. There are also some difficulties when either self-maintenance or third party maintainers are brought in and try to manage the administration of that warranty, because you can get into some issues of who is responsible for which piece of the problem.

But the contracts are not well-suited to continuing obligations beyond final payment.

Senator **Cohen**. Could I just interrupt here and ask a question? How would you handle a situation where you have a warranty of an O-ring and you have a shuttle that goes down as a result of a faulty O-ring that was not fully inspected? Do you have recovery against the company for the loss of the shuttle?

Mr. **McGowan**. Well, I think it is a pretty good example of the difficulties of trying to go back and assess responsibility and remedies. That system has not worked. I would argue that that was not a commercial O-ring to begin with.

Mr. **Fluke**. I think that is an important difference. The shuttle, of course, is a development item. It is not inappropriate that the body of DOD, like Federal acquisition regulations, be applied to the acquisition for not only that finished item, but a lot of the stuff that goes into it.

There are not a lot of places you can go and buy an off the shelf, 2½-million-pound thrust solid rocket. These are just not common items. I will not speak to my own personal view as to the responsibility of the contractors involved there; that is a different issue.

In the case of a much smaller O-ring that you might find in the fuel management system aboard a commercial jet, where there was an experience here not long ago where there was a failure of such O-rings, there is a case where the warranties, whether or not they allowed or provided for consequential damages to be paid by the suppliers—and am not familiar with those warranties—but if it is a routine failure that simply made the airliner not be able to leave on schedule, as opposed to a catastrophic failure, then clearly the O-rings and perhaps some of the immediate consequential costs like taking the fuel management system apart, replacing the O-rings, and putting it back together, might very well be borne by not so much the O-ring supplier, but perhaps the supplier of the finished fuel management system, say Hambrill and Standard, for example, supplying Pratt & Whitney fuel management systems.

Senator **Levin**. And the existence of that warranty in the commercial world is a tremendous incentive for good quality; is it not?

Mr. **Fluke**. Absolutely.

Senator **Levin**. And we do not utilize that with NDI's in the military procurement system very readily. There is a real resistance to it for a number of reasons, and it seems to me it is worthwhile pursuing that, because some of the reasons are legitimate obviously. Maybe there is a ship off at sea somewhere and it will not be very useful. But that is true in the private world, too, with a lot of items.

Mr. **Fluke**. Sure.

Senator **Levin**. But there are some reasons why it is not used which seem to me should be overcome—pure bureaucratic inertia, as you described it, an officer who wants to be finished with the item personally and get on to the next one, he wants to accept it—what were the words?

Mr. **McGowan**. Inspect, accept and pay, and go on to the next item.

Senator **Levin**. And that is it. Well, I do not think we can accept that as a reason not to use warranties, which can be an important solution to one of the problems that you have with commercial items being supplied to the Government.

Do you have any additional questions?

Senator **Cohen**. An additional comment.

As far as the problem about certification, I think Congress has some responsibility for it, because we hold hearings from time to time, and we are always attacking various agencies for not getting more and requiring more from individual contractors. So, I think we have a measure of blame to accept for perhaps some of this over-regulation, where the agencies take our concerns and then perhaps become a bit zealous and translate that into regulatory form.

But I think many of us on these various Committees are saying, "Get some certification here as well." And so these hearings also provide us with an opportunity to see whether we have gone too far, whether we are applying the right remedy to deal with the problem.

So, I thank all of you for being here.

Senator **Levin**. I would concur with what Senator Cohen said. We are indeed responsible for part of this problem. We also tried to put in place, a few years ago, a remedy for the bureaucratic overkill that, in part, we created. We do indeed frequently overlook our own responsibility for some of the things that we sometimes criticize.

But we did try to move the DOD and I agree with you also. It is not the only agency that does this. But we tried to move the DOD back towards the use of commercial items a few years ago. It has not worked apparently.

Even though the amendment was adopted to give them a push in that direction, the results are not readily ascertainable and I think we have an obligation, and this Subcommittee will seek to carry out that obligation, of seeing where we could meet with the industry, where we could meet with the DOD, pull together, if possible, some changes in DOD behavior which does not need legislative mandate. They already have plenty of authority to move in this direction because of the law we adopted 3 years ago.

But if they will not and if—if, in our judgment, it is bureaucratic inertia that is the cause of their failure to move after this kind of a meeting, which we intend to pull together—and we are going to have another hearing where the DOD can be heard in early June—then it will be our responsibility to try to act. And then that gets us into the question of whether we are micro-managing the DOD again, and whether or not we are changing procurement practices again.

One of the things industry has told us is, for God's sake, do nothing. You have already reformed and reformed the reforms, and then reformed the reformed of the reforms. So, our advice to you for your action is, do nothing for awhile. Let this thing settle.

On the other hand, this is a situation this morning, which I find disturbing—and obviously, we had this hearing because we have not found a response on the part of the DOD to an initiative of a few years back, to use more NDI's and we are going to continue to press for it.

So the next step will be an early June hearing where the DOD will be giving us their side of the story. My hunch and my hope is that DOD will say that at least there is good cause for us to be concerned, and this is what they will do to try to move further along this road. Perhaps they will tell us we are just on the wrong track and everything they are doing is just fine. We do not want to prejudge it.

But we are going to continue to move down this road because it makes no sense for us to be doing some of the things we are doing. I do not think anybody in the DOD is going to justify a 2-inch proposal for a $200 buy, which costs the customer or the supplier of DOD a heck of a lot more just to read the darn thing than they could possibly make out of it.

It does not make any sense for us to say you can buy the whole commercially, but you cannot buy a part of the whole commercially. And so we require you to buy the whole in a kit form, throw away—whatever the term is—what you are not looking for and just use the few pieces you are looking for.

Those are absurdities that I hope we can correct without creating other absurdities in the process. That is our goal. We are grateful to this panel and to the other panels that have come forward.

Mr. FLUKE. Mr. Chairman, one final thing that I think would be helpful in dealing with the DOD's presentation in June is, I think there is a lot of prospect for confusion between nondevelopment items and development items in their response to your questions. I think it is extremely important to make it clear, in the case of each question you might ask them, are you referring to nondevelopment items or to development items because there are two different answers.

I would have to say, in spite of you criticizing yourselves, that in the case of development items, perhaps the kind of oversight that you have been trying to do is not an overkill, by any means. In the case of the procurement of nondevelopment items, however, you cannot apply that same need for careful scrutiny and expect to get a similar result.

The system on the nondevelopment side is somewhat self-scrutinizing. It does require attention. But it is a lot more self-scrutinizing than the development item side is. So, separating the thought process in the question and answer process into those two realms might help a lot.

Senator LEVIN. That is a very important point and we will adopt it.

[Whereupon, at 12:15 p.m., the Subcommittee was adjourned, subject to the call of the Chair.]

DEPARTMENT OF DEFENSE'S INADEQUATE USE OF OFF-THE-SHELF ITEMS

THURSDAY, JUNE 1, 1989

U.S. Senate,
Subcommittee on Oversight
of Government Management,
Committee on Governmental Affairs,
Washington, DC.

The Subcommittee met, pursuant to notice, at 9:33 a.m., in room SD-342, Dirksen Senate Office Building, Hon. Carl Levin (Chairman of the Subcommittee) presiding.

Present: Senators Levin, Bingaman, and Cohen.

Staff Present: Linda J. Gustitus, Staff Director and Chief Counsel; Peter K. Levine, Counsel; Mary Berry Gerwin, Minority Staff Director and Chief Counsel to the Minority; Frankie de Vergie, Chief Clerk; William Luke, Warren Reece, and Melinda Loftin, Majority Professional Staff Members; Sean McAvoy, Minority Professional Staff Member.

OPENING STATEMENT OF SENATOR LEVIN

Senator Levin. Good morning, everybody.

Two weeks ago, we began our hearings on the Department of Defense's use of off-the-shelf items with testimony from a number of contractors who described the obstacles that their companies have encountered in trying to sell commercial and off-the-shelf products to the Pentagon. These witnesses expressed great frustration with DOD specifications, DOD regulations, and with the contracting process generally.

Bob Rossow of the Michigan-based Midland Brake Company testified about complex DOD specifications that often prevent commercial manufacturers from bidding on or winning DOD contracts. One example of such over-specification was the Defense Department's requirement of elaborate packaging which was not required for commercial customers but which cost $2 for a 5-cent part. Since we heard Mr. Rossow's testimony, other contractors have come to us with additional examples of over-specification by the Department.

Just yesterday, for example, we received a copy of a 37-page military specification for residential heat pumps. We are told that the Defense Department has just finished revising the specification and has managed to shorten it from 37 pages to 36 pages. The commercial manufacturer who provided us with these specifications told us that its commercial products meet the Department of Defense's needs, but it just simply cannot possibly comply with those specifications.

Even when the Department of Defense does decide to buy a commercial product, it frequently drives away commercial sellers by imposing burdensome and unnecessary contract requirements. At our last hearing, I presented the results of the Subcommittee staff's review of six solicitations for the commercial purchase of oscilloscopes. The staff found extraordinary inconsistency in the contract clauses that were used; 171 contract clauses were included in at least one of the six solicitations, but only 27 were used in all six, although the subject of the solicitations was the same.

These results do not appear to have been caused by any differences in the subject of the solicitation, the oscilloscopes. Now, subsequent to that hearing, our staff provided an identical hypothetical situation to one contracting officer from each of the three services. The same massive inconsistencies resulted. Of the 140 clauses that were used by at least one of the three officers from those services, only 53 were used by all of them, 31 were used by two of the three officers, and 56 clauses were used by only one contracting officer.

These numbers do not even include so-called local clauses imposed by individual commands within each service. The Air Force contracting officer stated that he would impose an additional 29 local clauses; the Navy contracting officer would impose an additional 33; and the Army contracting officer would impose an additional 35. Each of the local clauses was unique to the service imposing the requirement.

Now, faced by these kind of contract requirements, a lot of companies just give up. Naomi Williamson of Honeywell's commercial aircraft division testified last time that her company walked away from a $100 million procurement because of the Defense Department's regulations which are just unrelated to the commercial world. Dan Pinick of Boeing stated that his company has been unable to sell the Pentagon essential spare parts to support the existing AWACs system for the same reason. So the Air Force has AWACs and cannot buy the spares. The company just cannot function with those contract provisions.

It is interesting to note that the Center for Strategic and International Studies recently completed a study in which it found that the number of firms competing for Defense Department contracts has dropped from 118,000 to 38,000 in the last 5 years.

The problems raised by these contractors are not new. We heard about many of the same issues back in 1986. We passed a law requiring the Defense Department to do something about it. Section 907 of the 1987 Defense Authorization Act requires the Department of Defense to purchase, whenever possible, "non-developmental items," or "NDI's"—items that are already sold in the commercial world or already in use by the Government.

The real problem is that despite that law, the Pentagon remains hooked on the old way of doing business. Instead of recognizing that the commercial products are fundamentally different from military-unique items and require fundamentally different purchasing methods, the Defense Department has tried to buy NDI's by grafting some exemptions and exceptions onto existing rules.

That just does not work. As long as contractors and contracting officers have to get waivers and exemptions to buy NDI's, the purchase of NDI's will continue to be the exception rather than the rule. Our objective should be to make it easier to buy NDI's than military-unique items, not harder. Procurement officials just should not be designing new products from the ground up when an existing product is already available to meet the Defense Department's needs.

Under the NDI provision, the Department was required to take two basic steps to reduce barriers to the use of NDI's. First, the Department of Defense was required to use performance specifications rather than design specifications whenever possible. This means that they are supposed to tell the contractors what the product is supposed to do, not how to build it.

Second, the Defense Department was required to identify and address regulatory impediments to the acquisition of NDI's. Where statutory changes were necessary to eliminate these impediments, the Department was supposed to recommend appropriate legislative language.

Despite this mandate, the congressional preference for performance specifications still has not been incorporated into the Federal Acquisition Regulation or its DOD Supplement. And at last week's hearing, our contractor witnesses could not think of a single contract clause that has been modified or eliminated as a result of our provision.

Moreover, despite commitments that the Department of Defense made in a 1987 report to the Congress, our Subcommittee has learned that a promised Department of Defense manual on NDI acquisition still has not been issued—number one, the promised manual still is owing; two, a promised revisions to the DOD Directive on commercial products has not yet been promulgated; three, a Department of Defense steering groups on NDI's has been disbanded; four, the single DOD staffer responsible for the NDI program has been assigned so many other duties that he has been able to devote only half of his time to NDI's; five, only about 40 minutes in the Department of Defense's 20-week training course for program managers has been devoted to NDI's; and, six, a DOD plan to conduct a series of workshops on NDI's at regional training centers has been cancelled.

The Pentagon is a big place, and obviously we are not placing all these problems at the feet of today's witnesses. As a matter of fact, Mr. Atwood is new to the Pentagon, just having arrived there a few months ago.

And as I noted at the last hearing, Congress is not blameless in these problems either. We have contributed, obviously, a share to them. The bottom line is this: That we have a new administration, and I hope we can get off to a new start in eliminating barriers to the increased use of NDI's.

It took us years to change the procurement culture to make competition in procurement the key to reducing cost and improving performance. Senator Cohen and I authored the Competition in Contracting Act, and that has helped to finally make some real progress in the area of competition. I am now convinced that it is going to take the same kind of effort to change the DOD culture in the area of NDI's. It is a task which is well worth the effort because the savings are immense.

Let me now turn to our ranking member, Senator Cohen, for his opening statement.

OPENING STATEMENT OF SENATOR COHEN

Senator COHEN. Thank you, Mr. Chairman. I do have an opening statement, but I think you covered all of the major points I wanted to touch upon.

I think it is clear from the recent hearing that we held—and I believe that there were DOD representatives in the audience taking notes on what the representatives in the industry were saying—that impediments obviously result in greater costs, more delays, which are then translated into higher burdens for the taxpayer. And we tried to examine the issue of whether or not these problems were unique to the Department of Defense. I suspect they are not unique to the Department of Defense. But in view of the fact that Congress has mandated changes for removing the impediments to DOD's acquisition of NDI's and in view of the size of the procurement budget and responsibilities of the Department of Defense, it is all the more imperative that we try to find out whether or not these impediments can be successfully removed; and if so, why they have not been removed to date.

Now, there is the issue that some products are obviously unique requirements to the military, and there is no commercial marketplace to test both the price and the quality of those products. We have to always be mindful of that, and thus we need an elaborate system of regulations and monitoring activities to make sure that the taxpayer is getting not only a good product but the best product that we can get at a fair price.

I think the problem has been that this approach has permeated all aspects of DOD purchasing, not only in areas of unique military requirements, but also in areas where we can take advantage of commercial products at a better price and save the taxpayers some money. I think there is perhaps some merit to the industry's claim that we need a major change, not only in regulations and laws as such but also in attitude.

Senator Levin just mentioned that, initially, back in, 1981 when we first started the hearings on competition in contracting, there was a major objection and resistance to the notion that Congress is once again going to intrude into an area that was the exclusive domain of the executive branch, and particularly the Department of Defense. As a result the Competition in Contracting Act even given the fact that it does have its imperfections, as any law does, we have saved literally billions of dollars in DOD purchasing. I think that the same attitude perhaps can be found here, and we need some major changes in our approach to this particular problem.

I also want to sound a word of caution. I think it is important that we not over-react. There are important safeguards that we put into laws and for a good reason, and I do not want to see the Defense Department or other agencies caught in a cross-rough of criticism. On the one hand, we castigate you for not turning to the private marketplace to get more products at a lower price; and then when we find that there has been evidence of fraud and abuse, we then come back and say: Why weren't you more vigilant? I think that as we try to provide this change in attitude we so that take greater advantage of commercially available products, we also ought to make sure that we do not over-react and take out some necessary safeguards.

That is the spirit that I hope we will go forward with this morning, Mr. Chairman.

[The prepared statement of Senator Cohen follows:]

PREPARED STATEMENT OF SENATOR COHEN

Mr. Chairman, I thank you once again for holding these hearings on DOD's acquisition of non-developmental items.

On May 16, we heard from a variety of industry representatives that NDI acquisition has not received the attention it deserves from the Defense Department. The testimony we heard at our last hearing amply illustrated that the road is still fraught with a myriad of obstacles for commercial vendors trying to sell their products to the Government. Overspecification, unnecessary contract clauses, requirements for cost or pricing data, and a number of other impediments still plague the relationship, between the Department of Defense and commercial vendors. Allowing these obstacles to continue can result in higher prices and long delays in delivery times for the Department, and in turn, the taxpayer. While there have been some efforts by the Department of Defense to remove the impediments to the purchasing of non-developmental items since the Congress expressed its preference for NDI items three years ago, it appears that, by and large, there has been little done to change business as usual when selling to the Pentagon.

Today, we will hear the Department of Defense's response to the contentions and recommendations made at our last hearing. As I stated at the time, it may well be that problem of discouraging commercial vendors from doing business with the Government is not unique to DOD. Since the Congress has directly mandated the Secretary of Defense to act ro remove the impediments to NDI, and the Department's purchasing needs dwarf those of other agencies, it is appropriate that we review how much the DOD has done to improve its NDI efforts.

To date, much of our oversight and procurement reform efforts have been directed at that part of the Defense procurement system where the Department's needs differ significantly from the way business is done in the commercial marketplace. Because there is no commercial market to test the price and quality of many military products, it is appropriate to have an elaborate system of regulatory requirements and monitoring systems to insure that DOD pays a fair price and receives a quality product. In short, the Government has every right and obligation to require enough information to be sure that it is not being cheated.

Unfortunately, it appears that this same elaborate system of requirements has permeated those areas where the Department of Defense can buy commercially produced products in the competitive marketplace where prices and quality are competitively established, and where DOD requirements are often unnecessary and redundant.

Industry has told us that major regulatory changes are necessary to encourage NDI acquisition. Even more, industry charges that the entire mind-set at the Department of Defense must be changed, and that initiative and imagination need to be recognized and rewarded throughout the procurement system. Only a few years ago the concept of competition in contracting was largely alien to the Department. With much prodding and legislation by this Subcommittee and the Congress, competition has become an accepted precept of procurement policy and the dollars saved to the taxpayers through competition have been tremendous. Similarly, the prospects for savings through use of commercial products can be dramatic.

I look forward today to hearing the Department's side of this story. It would certainly appear that on this issue there is not only ample room for improving the current system's performance, there is also ample room for agreement about the need to do just that. We must, of course, be careful not to overreact, and eliminate necessary safeguards to ensure that the Government is not being overcharged or defrauded by its suppliers. I am confident, however, that by working together, the Congress, the Department of Defense, and industry can remove the current impediments to NDI acquisition. A streamlined system for the acquisition of these products would both improve the quality of the products procured for the men and women in our armed services and lower the ultimate price to the taxpayer of the Nation's defense. Now who could argue with that?

Senator LEVIN. Thank you, Senator Cohen.

Senator BINGAMAN. Mr. Chairman, I do not have an opening statement. I compliment you on holding these hearings. I think you have obviously done a tremendously good job of preparing these hearings, and your staff is to be complimented as well. I look forward to the testimony.

Senator LEVIN. Our first witness has brought to his task an extraordinary talent. This Government is better off because you are here, and we are better off at this hearing because you are here. We welcome you, Don Atwood.

If you would, summarize your testimony if you can. The entire statement will be made a part of the record.

TESTIMONY OF DONALD J. ATWOOD, DEPUTY SECRETARY, U.S. DEPARTMENT OF DEFENSE

Mr. ATWOOD. Thank you, Mr. Chairman, Senators.

I welcome the opportunity to be here. It is a subject which is very close to me, partly because of my background in industry and partly because of the challenge that I feel as we get into the details of acquisition within the Department of Defense.

I did prepare a statement which, rather than read, I request that it be made a matter of the record.[1] With that in mind, let me just say a few opening comments before we get into some of the questions.

I strongly favor, and I cannot emphasize heavily enough, increased use of commercial products throughout the Department of Defense. We have so much to gain both in the avoidance of cost for development of new products and in the logistics and maintenance of those products, particularly if they are available in the commercial sector.

Having said that, I can think of an outstanding example that we use, that Senator Levin and I were both a part of, and that is the procurement by the Army of the CUCV vehicles from General Motors over the past 5 or 6 years. This could have been a brand new development. Instead, they requested and we proposed a modification, a relatively minor modification, of a commercially available truck and, as a result, saved almost the entire development costs that would have gone with it. We manufactured those vehicles on the same line that the commercial vehicles were manufactured on, so that if you went through the manufacturing plant in Flint, Michigan, you would have seen commercial vehicles and military vehicles coming down the same line. Modifications were made to those commercial vehicles to adapt night running lights and for a different brake fluid that was required. Basically a tremendous amount of effort and strain was saved in terms of development, long-range maintenance and logistics. Furthermore, it took advantage of the years of reliability and quality enhancements that had taken place. We need to do much more of that. That is an excellent example of where it works well.

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[1] See p. 191.

Unfortunately, based on the evidence that you heard at your previous hearings and those that you just mentioned in your opening remarks today, Mr. Chairman, there are too many cases where we have not done that. With the staff at DOD, I can only pledge to you that we will review some 50,000 specifications that are out for procurement. We will review them in great detail with the idea of making use of commercial products wherever they are available.

Now, I want to urge some caution on our part, as Senator Cohen mentioned. We have to protect the Department. In any commercial product that is very loosely worded, some organizations can meet that very loosely worded specification, and we are all the worse off for it. So, with not going overboard in mind, we need certain specifications prepared for all products. There is no reason why we need to have a 37-page document to describe something that is commercially available on the open marketplace.

I pledge to you great support in all that effort, and I know the entire staff at DOD is behind me. One of the hallmarks of the studies that have been made, both by Congress and by the Packard Commission, is to encourage greater use, wherever available, of commercial products in all our applications. We intend to see that that happens.

Senator LEVIN. Thank you, Mr. Atwood. Your statement was a thorough and a thoughtful one. Your written testimony will be made part of the record, indeed.

I would like to make available to you a little survey that our staff did in preparation for this hearing, where we gave the contracting officers from each of the three services the same hypothetical purchase, and we ended up with a wildly different variety of contract clauses. The numbers here I mentioned before, but 140 contract clauses were used by at least one of the three, but only about a third of those were used by all three. This was for the same item, and that was very similar to the oscilloscope example that came up last time.

I think the cautionary note that you sounded and that Senator Cohen sounded is clearly appropriate. We obviously do not want to open ourselves up to abuse. The easier thing for contracting officers just to CYA, or CTA I guess it would be——

Senator COHEN. Do you want to be more explicit?

Senator LEVIN. Just to cover their rears, just will use endless numbers of contracting clauses which are needless. We know they are needless because other contracting officers for the same item will not use them. But when you think about the fact that two-thirds of the language in a contract which is used, once the decision has been made to go commercial, is extraneous or needless, at least in the eyes of some of the contracting officers, we have a problem which is curable, still protecting the interest of the Government against the fraudulent purchase or the sloppy purchase or the description which is so broad that it lends itself to abuse.

We are going to supply you with those two examples because it seems to me that you can really focus on the issue by looking at those two examples, where we have massive inconsistency between three contracting officers purchasing the same item commercially.

Senator COHEN. Would you yield for just a point?

Senator LEVIN. Sure.

Senator COHEN. We had testimony, Mr. Atwood, at the last hearing, in which industry officials indicated that a standard form Government commercial contract might include perhaps 15 to a maximum of 20 clauses to comply with all the applicable statutes. In your experience in business, is that something that you could lend support to, or is that perhaps an oversimplification on their part?

Mr. ATWOOD. I do not think oversimplification exists when we are dealing with a great majority of these items. It would certainly be an oversimplification if we were buying a new missile. But that is not what we are talking about, obviously. We are talking about items that are potentially available.

The only thing that I would guard against is the availability for abuse of those clauses in which some suppliers could find a loophole. We just have to be smart enough to foresee those loopholes. But the more the simplification, the better off it would be.

Senator COHEN. I think we also have to be careful of the impulse to say that we could put it all on five pages. You could put a contract together that would incorporate by reference every single statute and regulation on the books and say look how simple this is, I have got five pages here; and then you go to the industry representative and say all you have to do is sign this contract, and, lo and behold, he suddenly has got 30,000 pages he finds he has to comply with.

The notion that you can put it all in 15 or 20 clauses does not necessarily mean that it is going to be that simple.

Mr. ATWOOD. There would be more backup material with it, I am sure.

Senator LEVIN. After this hearing is over, would you take a look at the example that our staff presented to those three officers, those three contracting officers, one from each service? And would you and your staff get back to us with what you consider to be the appropriate contract?

Mr. ATWOOD. I would be pleased to.[1]

Senator LEVIN. It is probably going to be, if we look at this statistically, somewhere about a third to half the length of what it ended up. We think that that is where it will end up, just by the differences, the vast differences between the contracting officers.

There are surplusage in there in the eyes of two of the three officers, massive surplusage. And if you could just use that as an example, because it is something our staff is familiar with, and give us what you or your staff think would be the ideal. I think that it would be a great learning experience, frankly, for all of us to be working on the same contract. Let us pick out a couple contracts, go through them, your staff, our staff, and see what can be eliminated, and then work towards that standard contract. It may not be 10 clauses. It may be 50 clauses. But whatever it is, whatever is needed, it is going to be, probably, I think statistically, from our experience, about a third to a half of what is currently in these contracts.

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[1] Mr. Atwood has informed the Subcommittee that his office will work with the Subcommittee staff on this matter.

Mr. Atwood. We would be pleased to do just that.

I might add two comments relative to it. First of all, it may reflect also the fact that there is a lot of work to be done in fully implementing the Packard Commission and strengthening and stabilizing the uniformity of all of our purchasing policies and procedures through the Under Secretary for Acquisition. We are bound and determined to do that. So I suspect if you see variances, those are things that are the Under Secretary's job, that is to see that we do have standardization.

The other point is that in view of the visibility being given to fraud or potential fraud in the acquisition system, there has been and is a natural tendency on people's part to bend over backwards to make sure it could not happen in this particular procurement. We see a little overreaction because of the recent visibility, and I am sure you recognize that.

Senator Levin. The Congress has expressed a preference for the purchase of NDI's or commercial items. We did it in a 1986 law, and the response has not been very good so far. The provision in the law that the DOD use performance specs rather than design specs whenever possible has not been incorporated into the Federal acquisition regulation or into the DFARS. Would you review this issue, and would you take steps to ensure that our preference, the law's preference, for performance specifications is incorporated into the Department's rules and procedures?

Mr. Atwood. I certainly will.

Senator Levin. And could you do that within the next 6 months, or give us some reasonable time period so we can give ourselves some milestones here?

Mr. Atwood. Let me look at it, and let it sit at 6 months. If it is not satisfactory, I will get back to you.

Senator Levin. That is fair. That would be fine.

Mr. Atwood. I would either request an extension or say we can do it faster than that.

Senator Levin. That would be great if you would do that.

You referred in your testimony to a DOD program to review specs and standards that are 5 years old, and that sounds like a great idea. As you point out, action has not been taken on about 5,400 over-age documents.

In November of 1988, Under Secretary Costello reported that DOD policies on specifications and standards are oftentimes only paid lip service because each military department and agency seems to lack an office with sufficient authority to enforce implementation of policy. The excuse is frequently made that there are insufficient resources to implement policy.

Have you given any consideration to the authority that is necessary to accomplish the task and what office it ought to be vested in?

Mr. Atwood. I have not given it a detailed review to the extent of making a recommendation yet. However, within the framework of what we are trying to accomplish in standardization within the whole acquisition system under the Under Secretary's purview, indeed, the first reaction is that that is where it should be done.

There is a problem involved, and that is the effort which has been put on this task has not been sufficiently great to accomplish it in a time that apparently the Department had previously thought it would. We are taking a look at augmenting that effort.

Senator LEVIN. Can you let us know for the record where you are going to place that responsibility?

Mr. ATWOOD. I will.

[The information referred to follows:]

STANDARDIZATION EXECUTIVES

Standardization executives have been appointed as follows: Army: Mr. Donald Griffin, U.S. Army Materiel Command; Navy: Mr. Gerard Hoffmann, SECNAV (SPECAG); Air Force: BG John Douglass, SAF/AQX; and Defense Logistics Agency: Mr. Henry Filippi, DLA-SE.

Senator LEVIN. Okay. In your prepared testimony, you outlined six broad areas where you say action must be taken to restore credibility in DOD's specs and standards. Do you have a timetable for addressing those areas that you have outlined for us? Or if you do not have it at the top of your head right now, would you give us for the a record a timetable for that 6-point program to be implemented?

Mr. ATWOOD. I will do that, too, and give you a firm timetable on it.

Could I go back to something that was said earlier and I let slip by because I thought we were going to have an opportunity to comment on it?

That is, there has been much discussion in previous meetings, and today even, on telling the vendors what we want and not how to build it. We should be very careful because often the specifications are written such that they avoid telling people how to build something, when, in fact, the process is the net result of what the problem may be.

Let me give you a routine example. We could specify a gas bearing, that it have certain dimensions, a certain capability and a certain lift and speed and operating characteristics. And yet the processing which goes in to making the surfaces of the gas bearing, indeed, would have a variable effect on it. We need to be careful that we do not avoid the process. I am not saying that as a general rule, but there are times when we need to specify process.

Very often, for instance, when a purchase is made on the outside, the material comes in into your incoming inspection, it passes, but if they have made some insidious change in the process, it could take some time before the change is caught.

Senator LEVIN. I think there are obviously such cases. However, there is a massive number of buys, perhaps the majority, which can be made commercially.

Mr. ATWOOD. Absolutely.

Senator LEVIN. Yet, we add requirements which are completely just not capable of being met by commercial suppliers.

Take a look at those 37 pages of heat pump specifications. A major supplier of heat pumps just cannot deal with it, simply cannot deal with it, and will not bid.

Mr. ATWOOD. No. I understand, and I agree with you.

Senator **Levin**. It seems to me what you should do—and it takes time, and you have got an unbelievable amount of things on your agenda. But if we want to get to this item that is going to save us billions, if you want to get to this item, you ought to take some real examples of real people, real commercial people. Call them and say, okay—this company happened to be Honeywell on the heat pumps. Okay, Honeywell, you tell me what in those 37 pages of specs you cannot live with and why, and then you press your staff and say, now, why are we imposing 23 of those pages of contract provisions. When we decide to go commercial, we are going to lose bidders because they cannot comply with these; they are unable in their commercial world to do this. Then pressure staff.

I think it is going to take, though, you personally getting involved in some specific cases with the commercial world. Have them identify a couple cases for you. Put some burden on them. They are sitting here in the audience. Say, okay, pick a couple cases. I will take an hour out of my day. I will invite a couple of representatives in, look at specific specs—or contract provisions, because we are talking about both, both the situation where we have "over-spec'd" and where we have got too many contract clauses once we have decided to go commercial. Both situations are a problem.

But if you would do that, if you could just—and, again, I think I understand the kind of crunch that you have time-wise—but I think you should get inside one or two of these contracts and then tell your staff this has got to change, we have got to change the whole environment in which we work. That is what it is going to take. Once we decide we are going commercial, we have got to go at it—not as an exception, not as an exemption, not as a waiver to the usual rules, we have got to go at it a different way that is more relevant to the commercial world.

If you can just do that, I think we will make a lot of progress.

Mr. **Atwood**. I accept that, and I accept it willingly because probably 1 year ago I would have been on the other side of the table.

Senator **Levin**. My time is up. Thank you.

Senator Cohen?

Senator **Cohen**. Mr. Atwood, one of the problems that we hear complaints about frequently is that of the lack of uniformity. In another context, for example, Senator Levin and I were involved back in the early 1980's, in dealing with the debarment issue. At that time, we found that a contractor who had been found to be either guilty or accused of having engaged in fraudulent conduct could only be debarred from doing business with a specific agency, but could then turn around and walk across the street to another agency and be completely free to engage in the performance of other Government contracts. We felt there ought to be some uniform application of the debarment stamp of disapproval.

I think, the converse is true here, in that many of the industry representatives come in and say, look, on the one hand we go through this process and we get stamped with approval by the GSA, and then we have got to go through the same process with DOD all over again. This is simply unnecessary, redundant, duplicative and it is costly and really quite unsound.

Now, assuming there are no unique aspects to that particular product, do you feel that if you have one agency gives its stamp of approval, that that ought to be sufficient?

Mr. ATWOOD. I would like to give a little more thought to that answer than off the top of my head, if I could, Senator. The reason is I am not familiar with what another agency outside of DOD would impose for a restriction or regulations in order to certify a company to do business with the Government.

Senator COHEN. Again, the qualification is that there are no unique military specifications involved.

Mr. ATWOOD. That is the part that I do not know. But, assuming that, in essence, if they were to do business with another department and that it satisfies all the requirements that DOD would have imposed, then I have no problem with it.

Senator COHEN. But that raises the issue of whether the requirements of DOD are excessive.

Mr. ATWOOD. And we need to look at that.

Senator COHEN. You cannot say that, well, if they do everything that we would have done, there is no problem.

Mr. ATWOOD. Yes, and we need to look at that.

Senator COHEN. But the question is: Are you requiring more than is necessary?

Mr. ATWOOD. That is a finite probability that we are, and we need to look at it.

Senator COHEN. At the last hearing we had, industry proposed the creation of an additional waiver for so-called flow-down requirements. Like OFPP's draft legislation that is being reviewed at OMB, it would significantly reduce some of the impediments that industry finds. It would remove some of the disincentives that exist for both the prime and the subcontractor when taking on Department business.

There is a problem here in that Congress has used the procurement process to achieve certain socioeconomic goals because it believes that it is important that we promote those goals and adhere to them. Now, if a contractor does business exclusively with the Government, they have to comply or he has to comply with anti-kickback provisions, equal opportunity, affirmative action for handicapped workers and others.

Do you think that commercial vendors ought to be exempt from these provisions?

Mr. ATWOOD. No. Let me make a comment on this in general. I think the commercial industry, industry in general, does an outstanding job. They have done a good job in taking advantage of the capabilities that exist in a number of companies that do not have the staffs to live up to all of the agreements and all of the rules and regulations that perhaps a larger company has by definition. They offer work to disadvantaged companies and to companies that are in a location where there is a socioeconomic problem that needs to be solved. I think private industry has done a good job at that.

There is a question in my mind as to the role of the Department of Defense in that area, and, therefore, any special rules or provisions should be looked at very carefully before we undertake that, at least in the Department of Defense's view.

I might feel one way—and if I went ahead and did that, I think Congress would be all over me for having not lived up to my responsibility to the Department. So we want to go very carefully in any area like that.

Senator COHEN. Industry officials also urge that you make greater use of commercial warranties, and greater use of commercial inspectors. What they fear is that in doing business with the Government, suddenly inspectors from DOD come swooping in and find some deficiency and shut down the plant. And they do not want to risk that kind of action.

Question No. 1 is: Do you think that commercial inspections are sufficient in most cases and could support an expansion of using commercial inspectors?

Then, No. 2: On the question of warranties, I think you point out in your statement that commercial warranties tend to be parts, warranties as far as they are free from defects, they do not warrant performance. Do you think that industry itself would be willing to switch and perhaps give a guarantee of performance as opposed to the warranty of the parts themselves simply being free from defects?

Mr. ATWOOD. Let me take your questions in reverse order, if I could, and talk about the warranties first.

I have no problem—and I can speak from an industry standpoint also—in warranting the full performance of something for use by the military. There are two difficulties that arise. Generally speaking, if something is warranted in the commercial world, there are locations where that warranty service is done, or there are inspection facilities where it is done. DOD is a worldwide operation, and very often we are dealing with companies that are restricted to, if not just the United States, then to some geographic area within the United States. So that becomes a problem.

The other part is that generally a warranty given by industry on its products is tempered by use. And, certainly, the DOD does not want to be restricted in how it uses many of its products. So we would have to temper that.

Having said those two warnings, I think industry would be very receptive to consideration of warranting its product after delivery. I think that is a practical thing.

Now, the first part of your question had to do with——

Senator COHEN. Was on inspectors.

Mr. ATWOOD [continuing]. Yes. This has been a serious bone of contention with many people, including myself. I have seen commercial lines parallel with military lines in the same building, and I will give you an example that had nothing to do with the company I came from. In Evandale, Ohio, General Electric makes jet aircraft engines for the commercial world and for the military. They will tell you that on the military line they almost have one-to-one correlation of their manpower with Government inspectors, Government auditors, Government test people, Government reviewers, just making sure that they do not do anything wrong. And for the commercial line, they do not have a single airline representative or a single airframe manufacturing representative on it, and yet they are producing essentially the same engines.

So we need to review that. That, to me, is just unforgiving. We are treating the company as though they are inherently dishonest, yet in the commercial world, they treat them like they are inherently a high integrity company that is providing an end product at a given cost. It does not make sense to have that wide a disparity in the inspections.

Senator COHEN. One of the other complaints we had several weeks ago had to do with cost pricing data. For example, you might have a situation in which the general contractor who has the contract with the Government is not required to submit this kind of detailed cost data and information, but the subcontractor is. The argument is that if the general contractor who bids on a basis of competitive bidding gets a contract and does not have to supply this information, why do we?

Now, I understand that the FAR regulations are being reviewed to simplify that process. Is that something that you support?

Mr. ATWOOD. Yes, I support simplification of it, with the idea in mind that, again, a contractor must select their subcontractors in a manner not dissimilar from the way they in turn, are selected. I think there has to be a degree of trust and cooperation.

One of the outgrowths of all of this—and you undoubtedly hear the very same thing—is the deep concern that I feel I share with all of you about almost a confrontational atmosphere that exists between much of the supplying industry, both the commercial and military industry, and DOD and Congress on the other hand. It is not a wholesome situation. We must deal at arm's length; we must deal with all of the proper precautions; but that does not mean that we cannot be good suppliers, good customers at the same time.

Senator COHEN. I just have one final point to make in terms of attitude, because that is equally important in trying to resolve some of these issues.

Senator Levin and I both service on the Armed Services Committee, and we both have been active in dealing with something called low-intensity conflict, another acronym, LIC, and SOF, special operation forces and so forth. While most of our military commanders have recognized that low-intensity conflict is probably the most likely type of conflict that we have to confront in the immediate future, they also say that it is the kind of conflict that we are least prepared to deal with.

We tried to confront that issue, and as a matter of fact, passed legislation over the objection of the Department of Defense to set up a special command for special forces, setting up within the Department of Defense an Assistant Secretary for Low-Intensity Conflict. We also mandated the creation of a coordinating board within the National Security Council.

The board, to my knowledge, has never met. They have never had a meeting to see if they can achieve the coordination that is going to be so important. I raise this in this context because DOD's letter to the Subcommittee explained that a steering group chaired by the Office of the Secretary of Defense to implement suggestions on commercial components was unnecessary. The group was established back in May 1987. It took no substantive action and was then disbanded.

It seems to me that there is an awfully close parallel between the attitude reflected that if we do not like the legislation we simply ignore it, and that is what took place with respect to low-intensity conflict as far as a coordinating board is concerned. And the same kind of signal, it seems to me, was sent to the procurement community that the NDI preference was not going to be a very high priority within the Department of Defense itself.

Now, I may have reached for these parallels, but that is the way it struck me.

Mr. ATWOOD. I do not think you are reaching at all. In fact, I just came from a breakfast meeting with Secretary of the Army Marsh. The subject was exactly your first point, the low-intensity conflict, and what do we do to better prepare ourselves for perhaps a changing environment as we look ahead. That is a very serious problem.

As far as the Department ignoring it, let me tell you a little story which I think best demonstrates what I am saying. We had the CEO of a very large company come in and talk to us during the time when we were initiating our management review, which is due out within the month. He was telling the things that he did in his organization to get it done, and someone from DOD said—I will not mention his name—"How could you be sure that the people did what you asked them to do?" And he said, "They worked for me." It was very simple.

In DOD, sometimes we ask people to do something, and that is the beginning of negotiation. So we need to make sure that we do a little internal discipline.

Senator COHEN. I hope you will take a look at that because I think the wrong signal is sent when a group like that in your office is simply disbanded.

Mr. ATWOOD. I am not familiar with the case, but I certainly will take a look at it.

Senator COHEN. Thank you.

Senator LEVIN. Thank you, Senator Cohen.

Senator Bingaman.

Senator BINGAMAN. Thank you, Mr. Chairman.

I understand the Defense Science Board has done a report on the opportunities for use of commercial semiconductors, computers, and computer software called the Burnette report. Several of the reports I have gotten from people who have been involved in it indicate it is an excellent report and would be very helpful to us here in Congress, but they cannot show it to us until it is briefed to Secretary Cheney and yourself. I was just wondering if there was any way you could expedite that situation so that we could actually see that report in time to take some of its recommendations, if it is appropriate, and do something with them.

Mr. ATWOOD. I would be pleased to, and I am setting up a review of the report myself. I have not seen it, as you perhaps know. But I will be getting a review of it and will review it with Secretary Cheney, too, and then make it available so that you see it.

I understand it is an excellent report.

Senator BINGAMAN. Everybody seems to think that, but I still need to find somebody who has read it.

Mr. ATWOOD. It may not look as good after we have read it. [Laughter.]

Senator BINGAMAN. We may never know.

How do we get uniform procedures in this area of buying of commercial products? How do we get uniform procedures across DOD?

Mr. ATWOOD. I think that is a valid question, and, of course, it goes back to the original establishment of the Under Secretary for Acquisition and his staff. The purpose is to ensure that among the Services in matters of policies and procedures and how we buy, that the Under Secretary has full authority to direct all activity to ensure standardization.

Now, it does not do much good to have standardization if we do not have the capability of understanding it. One of the things that perhaps will come out of this semiconductor report is that if we continue to say, although there are commercially available integrated circuits, we are going to impose unique DOD requirements on them so that DOD cannot use those commercially available ones, then indeed we have not accomplished much. So it is not a question necessarily of just standardization—although that is important. We do not want the Navy bound to one thing and the Air Force to another. It is important that we review these for standardization with intelligence and make maximum use of commercially available items; otherwise, we will have imposed a standardized system which is no better than the others.

Senator BINGAMAN. No, I understand that, and I understand that there is a lot of judgments to be made as to what is available commercially that can be used by DOD and what is not. But that is one problem, and the other problem is: once you settle on it, once you decide that there are adequately manufactured heat pumps on the market and DOD does not need to have its own heat pump design, then why cannot you have that decision be DOD-wide?

Mr. ATWOOD. There is no reason you cannot. And you should.

Senator BINGAMAN. There is another question that occurs to me in just hearing some of the other points being made. Is the right way to get at this to get out the 37 pages of Mil Specs and start going through them to see which of these things is actually necessary? Or is the right thing to do to start with the available products which DOD uses in some form and put the burden on someone to say why those products are not adequate to the job?

Mr. ATWOOD. I think your point is well taken, and probably we should do both. Earlier, I heard the suggestion that we should call in many of the commercial operators who have products that they feel satisfy the needs and review both, one versus the other, to make sure that we have not overlooked something, or that they have not overlooked something. So it is not just a question of DOD reviewing its specifications and reviewing them perhaps in a vacuum. We should review them with the knowledgeable input that comes from people in industry who make products that fill those needs.

Senator BINGAMAN. I am very untutored in the intricacies of this, but it seems that DOD might say that, for the following items the Department of Defense policy is to buy commercially available products, and then list items that an initial determination has been made that there are good, usable, commercially available products for those items. Then put the burden on any service or any part of DOD that wants to argue otherwise, put the burden on them to come forward to the Under Secretary for Acquisition and demonstrate that their needs are such that no commercially available product of that type will fit their demands.

I do not know. Is that too simple an approach to it?

Mr. Atwood. No, it is not too simple at all. In fact, I think we should do that and force anyone who is not going to buy to come back and tell us why they are not going to buy.

Senator Bingaman. On the issue that you raised, the example that you gave of performance specifications of the General Electric plant where they are making motors and engines for the commercial sector and for the Defense Department, and they have got all these people checking what they are doing on the defense side of the line. If you had the specifications that were performance-based rather than design-based, why would you need anybody to check it?

Mr. Atwood. I will not try to apologize for the way the Defense Department has grown in their inspections and so forth, except to say that we are dealing with taxpayers' money. There is a natural inclination on all of our parts to make sure that there is no way that we are wasting it or spending it foolishly. All of us in DOD need some form of a check and balance to ensure that, yes, we have investigated it and we see that they are doing it wisely; and that, yes, as these engines passed one point to another we did test them to make sure that it was done.

But perhaps we have gone overboard on that. In other words, I do not know that we can ever, unless it is a commercial product, get to the point where we do not have anyone in their plants. But perhaps we have gone overboard and have too many.

Senator Bingaman. Well, I guess the question, though, is: If it is a fixed price contract, if we are paying a set price for each of the engines that General Electric is making, and we have agreed as to the performance specifications that they need to meet with these engines, why can't we just check the engines?

Mr. Atwood. The answer is we can, but generally it is not as simple as being a fixed price. It is a fixed price negotiation, or it is a renegotiable each year, or we have specified more than just the performance because of some idiosyncrasy in the processing that we need to check. And that is how it builds.

But you are right. If something can be done by the airlines and something done by the airframe manufacturers with minimum sort of checks, then, in fact, you can get away with it. FAA does that. The FAA asks you to self-certify, and if you provide something over a period of time and their indication is that you are a reputable supplier, they will accept your own certification. And there is no reason we cannot do more of that.

Senator Bingaman. That is all the questions I have, Mr. Chairman.

Senator Levin. Thank you, Senator Bingaman.

Just a few more minutes. I know you are trying to leave as close to 10:30 as you can.

There was a draft DOD report which identified 18 specific impediments to the use of NDI's, and after substantial editing, the final report identified only 5 general issue areas. This was a 1987 report, and I am wondering whether or not you are aware of that report and the discrepancy between the draft report which identified the 18 specific impediments and the final report which just had the 5 general issue areas.

Mr. ATWOOD. I am not familiar with it, Mr. Chairman. But I will get familiar with it.[1]

Senator LEVIN. If you would, perhaps, provide that for us, it would be helpful.

Mr. ATWOOD. Yes.

Senator LEVIN. My next question relates to the manpower which is devoted to the NDI issue. Here is what our staff has learned about the Department's NDI program. First, the Department has dedicated only one person to the NDI program over the past 2 years, and for the last year, or most of it, that person has been assigned to so many other duties that he has been able to devote only half of his time to the acquisition of commercial products. As a result, the Defense Department still has not published the basic directive and manual on NDIs, that has been in draft form for about 2 years.

Second, the services have not done much better. The Army and the Navy have told our staff that they do not have any personnel that is solely devoted to NDI's. The Air Force was able to identify a total of 400 staff hours; that is about a quarter of a man-year that has been devoted to NDI since our bill was enacted a couple years ago.

So one of the important things that I hope you would do would be to look at the resource allocation on NDI's and let us know what you are able to do in that area.

Mr. ATWOOD. We will do just that. I discussed that yesterday with Mrs. Spector and Mr. Saunders, and clearly we have understaffed that activity. If we are to accomplish what I laid out earlier to you, then, indeed, we have to add some effort to it.

Senator LEVIN. Also take a look, if you would, Mr. Atwood, at your 20-week program management course where only 40 minutes are devoted to NDI's, and at your 1-week course on the fundamentals of acquisition where there is 15 minutes devoted to NDI's. The Army's and the Navy's and the Air Force's courses really are worse. In the case of the Air Force, they cannot identify any NDI training at all that it offers to its employees. So if you would, take a look at that also.

Mr. ATWOOD. I will take a look at that. We need to review also our entire training and qualifications for people in acquisition. It is critical that we re-emphasize the significance of that function within DOD.

Senator LEVIN. My final question is relating to an OMB directive. It is my understanding that the OMB—request rather than directive—requested more than a year ago that the DOD establish an information system to maintain some data on the use of commercial products so that we can get some idea as to what percentage of the products that we buy are commercial. It is my understanding that the Department has not yet taken any action on the OMB request.

Are you familiar with that?

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[1] See p. 222.

Mr. ATWOOD. No, I am not. But I will look into that.

Senator LEVIN. Would you get back to us on that?

Mr. ATWOOD. Yes.[1]

Senator LEVIN. There is a lot, then, for you to get back to us on. Senator Cohen.

Senator COHEN. Just one quick question.

Can you tell us what the timing is going to be for the release of the internal management review report that President Bush mentioned in his budget message to Congress?

Mr. ATWOOD. We are just about finished with it. Secretary Cheney and I will be reviewing it with the President probably this coming week.

Senator COHEN. Will that review address the use of NDI?

Mr. ATWOOD. Yes, it does.

Senator COHEN. Thank you. That is all I have.

Senator LEVIN. Senator Bingaman?

Senator BINGAMAN. Nothing further.

Senator LEVIN. Thank you, Mr. Atwood, again, for coming by and testifying.

Mr. ATWOOD. Thank you very much.

Senator LEVIN. We will be in close touch with you.

Mr. ATWOOD. And I will get back to you on these items that we have discussed. Thank you.

Senator LEVIN. Thank you.

Our next witnesses are a panel of two: Eleanor Spector, who is the Deputy Assistant Secretary of Defense for Procurement; and Gregory Saunders, the Assistant for Commercial Acquisition.

Mrs. Spector and Mr. Saunders, we welcome you. Good morning. We will put your statements in the record, and you can proceed to summarize them, if you would.

TESTIMONY OF GREGORY SAUNDERS, ASSISTANT FOR COMMERCIAL ACQUISITION, U.S. DEPARTMENT OF DEFENSE[2]

Mr. SAUNDERS. Thank you, Mr. Chairman and panel members.

I am pleased to have the opportunity to speak to you this morning about what I consider my program. I am the one person who has been assigned to work on commercial acquisition.

My name is Greg Saunders. I am a staff engineer in the Office of the Deputy Assistant Secretary of Defense for Total Quality Management. For the past 3 years, I have been the DOD's point man for commercial acquisition. I am responsible for initiating the actions to help move DOD in the direction of buying more commercial products. I have worked with two Defense Science Board Task Forces, including the one that Senator Bingaman mentioned earlier, and that task force we hope, is within weeks of issuing its report, the recommendations of which I expect to be charged with implementing.

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[1] Mr. Atwood has informed the Subcommittee that USD(A) will establish a database DOD-wide to trace our progress in expanding the procurement of commercially available products. Details on the database development will be provided to the Subcommittee staff as part of the 6-month post hearing review, requested by Senator Levin.

[2] **See p. 203 for Mr. Saunders' prepared statement.**

The 1986 task force observed that they could not address acquisition of commercial products without also discussing buying practices. Mrs. Spector will talk some about the buying practices. I would like to comment just briefly on how we arrive at our requirements.

In 1976, DLA conducted a test program called the Commercial Commodities Acquisition Program. We used simple purchase descriptions to buy a number of clearly commercial products such as gloves, towels, thermometers, x-ray film and mustard. The test was designed to validate certain assumptions about buying commercial, certain gut feelings, if you will, that we all felt were true, but had no data to support.

The test was successful by every measure. In 52 buys worth over $40 million in 1976 dollars, there were more bidders; product quality was equal or better in all but a very few cases; and in those few cases, the manufacturer corrected the problem once he was told of it. Prices were lower, deliveries faster, and awards to small business were up by 1 percent, not a significant increase but very significant in showing that small business was not harmed by this process.

Following that test, we institutionalized the development of the short purchase descriptions, which we called commercial item descriptions or CID's, and began an intensive program to replace Military Specifications. A key to the success of the program was a requirement that offerors be able to demonstrate commercial market acceptability. This essentially said that, in order to sell a commercial product to the Department of Defense, a manufacturer had to have a commercial product and had to be able to demonstrate that they sold that product in the commercial marketplace. This allowed us to substitute the rigorous test of commercial market acceptability for our detailed quality assurance provisions that we had traditionally written into military specifications.

We attempted to protect small business suppliers, or any suppliers, who had built their business around providing to military specifications by including a grandfather clause which allowed them to continue to offer and be evaluated against the old military specification for 3 years after the commercial item description was issued for their product. But, in 1983, such a supplier, seeing his business potentially evaporate, complained to his Congressman about the potential loss and was able to get a provision placed in the Appropriations Act that restricted our use of the commercial market acceptability. That destroyed the basis on which we were so successfully able to buy truly commercial products. It essentially removed "commercial" from our commercial acquisition program.

Although the restriction was removed in 1986, the Competition in Contracting Act with its emphasis on full and open competition has kept us from returning to the practice of requiring commercial market acceptability as a precondition for bidding. The ability to restrict competition for clearly commercial products to commercial suppliers seems logical and fair. It is necessary if we are to be able to continue to simplify our specifications and to encourage participation by top quality commercial suppliers.

We have, however, made some progress. We have expanded our use of GSA Multiple Award Schedules, and, in fact, we have a test going on now to expand into purchasing more complex, higher dollar value items such as construction equipment and materials handling equipment. We have greatly increased our participation with non-Government standards—writing organizations and have helped to start standard-writing committees in a number of areas, such as food and food products.

With the steps outlined in Mr. Atwood's testimony, we expect to make continued progress replacing military documents, eliminating outdated requirements, and stating our needs in terms of performance rather than excessive design detail. We will also continue to work toward proper selection of specifications and tailoring standards and statements of work to try to eliminate the problems such as Mr. Rossow described.

Finally, on the subject of the state of policy in DOD, we issued our first directive on commercial acquisition in 1978. Despite several tries to revise that policy, the 1978 directive is still in place. The current draft revision has been in preparation and coordination since passage of the NDI preference legislation. Recognizing that the DSB report and, more than likely, this Committee will give us some new guidance, we have decided to start over from a clean sheet of paper. My direction is to make issuance of that policy a top priority.

While policy is necessary, it is not sufficient to ensure implementation. Each of the services has issued guidance manuals, and we do have a DOD draft manual in the works. We have also recently issued a pamphlet describing a number of on-the-shelf commercially available data bases that help match requirements to products already available.

We have some success stories. We unfortunately have too many stories like those you heard at the earlier hearing. As a strong advocate, I sometimes have to remind myself that buying commercial products is not really the goal. The goal is to buy the best product for the job at the best price. Where that product is a commercial or non-developmental item, there should be no obstacles to attaining it. We will continue to work toward more complete implementation of NDI preference and elimination of barriers to use of commercial products in DOD.

Senator LEVIN. Mrs. Spector.

TESTIMONY OF ELEANOR R. SPECTOR, DEPUTY ASSISTANT SECRETARY FOR PROCUREMENT, U.S. DEPARTMENT OF DEFENSE[1]

Mrs. SPECTOR. I am Eleanor Spector, Mr. Chairman, and I am responsible for procurement policy in DOD. I am not responsible, however, for determining what we need to buy or how these requirements will be defined in specifications or statements of work. This seems to me to be the root of the problem in DOD's acquisition of commercial products.

I am not suggesting that there are not changes necessary to our rules to facilitate the acquisition of these products, and we now are considering changes to the FAR in one area that has been cited as an obstacle to buying commercial products; that is, our unnecessarily asking for cost and pricing data in certain circumstances.

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[1] See p. 209 for Mr. Spector's prepared statement.

The new coverage would further the policy to buy commercial products by relying on price analysis techniques rather than cost analysis to the maximum extent possible, restructure the designation of sales categories to broaden commercial exemption criteria, give the contracting officer greater latitude for judgment in determining whether a product is sold in substantial quantities to the general public, exclude predominantly commercial companies from submitting our 1412 forms, which is a claim for exemption from the submission of cost and pricing data.

These have been of great concern to commercial suppliers, and we expect the DAR Council to be reviewing these changes as early as this month. This we feel could be a significant change to removing an impediment to the buying of commercial products.

Many of the impediments that we see are not imposed by DOD. When you had your hearing with the commercial suppliers, Mr. Pinick of Boeing testified that 19 FAR clauses require flow-down to Boeing's vendors, and they inhibited the sale of a modified 757 aircraft to the Navy. All 19 of those clauses are required by statute. With each session of Congress, we see more and more statutes that make us less desirable customers to commercial contractors. An example: Procurement integrity, which applies to commercial products, and liquidated damages, which applies to commercial suppliers, that requires us to recover money if companies fail to meet their small disadvantaged business goals and do not use good faith to try to meet them.

The competitive procedures currently required by law were not designed with commercial products acquisition in mind. The current statutes seek to maximize competitions by ensuring that every source that wants to manufacture a product has an opportunity to compete, including small and small disadvantaged businesses, even when they do not have substantial sales to the public. Operating within those constraints, contracting officers find that detailed specifications must be adopted early in the acquisition process to assure that suitable products are routinely purchased.

Under the minimum needs doctrine that we have, where we are supposed to only define our minimum needs, we sometimes have to revise specifications to take account of knowledge gained through market research. Sometimes when we do that, we are accused of bias. Writing a specification around one commercial product can imply bias toward a particular supplier of a product.

To help correct some of these deficiencies, we have been working with OFPP to develop a draft bill to encourage requirements people to specify commercial items because buying them would be much quicker under this bill than acquiring a Military Specification item. Allowing the commercial marketplace to substitute for the very complex procurements system now required would certainly save time and money.

The purpose of the bill is to require the development of commercial-style purchasing procedures to better utilize market research, avoid over-specification, and otherwise facilitate the acquisition of commercial products.

That bill would provide a procedure for purchasing commercial items that approximates commercial-style acquisition. It would provide variations to those procedures which may be useful in procuring some commercial-type items, would provide greater authority to the contracting officer in establishing time periods for synopsis and receipt of offers, allow for awards based on best value, and award without discussions to other than the low bidder.

Procurements would be initiated with a public notice requesting interested sources to make submissions describing their products and explaining how they meet the advertised needs. The public notice would be issued as soon as the contracting officials were able to explain the needs in conceptual terms. Commercial products would be required to have achieved market acceptance and to comply with minimum fundamental requirements synopsized in the public notice. These could include commercial standards, minimum function and performance levels, essential form, fit, and function specifications, and, in appropriate cases, DOD manufacturing process qualification standards.

We badly need a bill of this sort, and, of course, Congress has to help us in obtaining it.

That concludes my statement. Thank you.

Senator LEVIN. Thank you very much, Mrs. Spector.

First of all, Mrs. Spector, a question for you. The testimony at our earlier hearing on NDI's indicates that we have a tremendous amount of inconsistency. Were you familiar with that testimony?

Mrs. SPECTOR. Yes, sir.

Senator LEVIN. Even without the elimination of a single statutory requirement—in other words, there are statutory requirements; we acknowledge that. We think you are wrong in terms of how many you have identified, but put that aside just for the moment. There are statutory requirements.

If we did not eliminate one of them, it would be of immense help if the DOD would develop a standard form contract for commercial purchases so that we would not have this tremendous inconsistency with some officers on the same item putting in 100 clauses, other officers putting in 50.

Mrs. SPECTOR. We are certainly going to consider what you recommend. We also reviewed the 140 clauses for the oscilloscope, and some of the findings are interesting on that. Let me give you one.

Twelve of the 16 unique Air Force clauses were required by regulation due to the dollar amount of the contract.

Senator LEVIN. We are not talking about the add-ons for each of the services.

Mrs. SPECTOR. Right.

Senator LEVIN. We are talking about the common clauses.

Mrs. SPECTOR. I think we will try to come up with something like that. It might be necessary to do so by type of contract. There are different clauses for different types of contracts. It might also be necessary at different dollar thresholds.

Senator LEVIN. How do you explain on the same purchase, when we give a hypothetical to an Army, Air Force, and Navy contracting officer, that they come up with wildly different contracts?

Mrs. SPECTOR. The research that we did on it showed—and this was not a hypothetical, but this was the example GAO had in its report—that the Navy, for instance, had different packaging and shipping requirements because of its sea use of these oscilloscopes. The Air Force's contract was the only one in the case that was looked at that was over $100,000, at which point certain clauses kick in. Some of it is not explainable, and some of it is not justified.

We will certainly look at it and try to come up with a more uniform set of requirements when we buy commercial products.

Senator LEVIN. In November 1987, the Department submitted a report to Congress on impediments to the acquisition of NDI's. The draft report stated the following: "That inappropriate and inconsistent contract clauses used by different Government agencies, different departments and agencies within the DOD, and different buying organizations within a department or agency cause confusion and uncertainty and increase the contractor's risk in doing business with the Government."

Now, that statement was omitted from the final version of the report. I take it you agree with the statement from what you just said. Do you know why it was omitted?

Mrs. SPECTOR. Sir, I do not specifically know why it was omitted, but I will tell you that when we have gone back to contractors and asked them which specific clauses are impediments to your selling to us—I know these numbers and these statistics are cited—the one that seems to come up all the time are our cost and pricing data provisions. The others were not cited to us specifically as to which were impediments. And in the cost and pricing data area, we are making some very dramatic changes to the coverage. I do not know why.

Senator LEVIN. Do you agree with the statement that "inappropriate and inconsistent contract clauses used by different Government agencies, different departments and agencies within the DOD, and different buying organizations within a department or agency cause confusion and uncertainty and increase the contractor's risk in doing business with the Government"? Do you agree with that?

Mrs. SPECTOR. I do not know which clauses they would be. I do not honestly know which clauses are causing that much confusion. I do not know the answer as to whether that is true. I know there are a lot of clauses——

Senator LEVIN. Well, when you have three contracting officers coming up with totally inconsistent contracts for the exact same item—and we went through that hypothetical, and my staff will share that hypothetical with you so you do not have a different quantity or anything like that. Can you possibly explain such wild inconsistencies?

I thought you just said that you think some of it is inexplicable.

Mrs. SPECTOR. Some of it is inexplicable.

Senator LEVIN. Some of it is inexplicable, not all of it?

Mrs. SPECTOR. Yes. We ought to correct that.

Senator LEVIN. If some of it is inexplicable, why do not we just acknowledge that in that DOD report? Why did that have to be watered down?

Mrs. SPECTOR. I do not know the answer to that. What I will say is that with 30,000 contracting people out there, unless you make the regulations so rigid and so burdensome, if you leave flexibility in the system, there will likely be inconsistencies. The question is whether those inconsistencies are driving people away from doing business with us. And I do not know the answer to that.

Senator LEVIN. Let me assure you, they are.

Mrs. SPECTOR. That may well be.

Senator LEVIN. Let me just assure you they are because we have had testimony here. I think you heard that or you are familiar with that testimony that says that. So unless we have got these contractors who are just simply coming forward and lying to us and we do not believe it—these are legitimate people who are saying they cannot deal with it. They are in the commercial world. They are given 35 pages of contract provisions which they cannot meet in their world. These are for items that we want. We are missing each other here. Have you met with people in the commercial world?

Mrs. SPECTOR. Yes, sir. Yes, I have.

Senator LEVIN. Have you asked them for——

Mrs. SPECTOR. Yes, I have.

Senator LEVIN. And they have not given you——

Mrs. SPECTOR. As recently as yesterday.

Senator LEVIN. Well, before yesterday, had you asked them for examples of what contract provisions that they are referring to?

Mrs. SPECTOR. Yes.

Senator LEVIN. And they have not given them to you?

Mrs. SPECTOR. They have said cost and pricing date provisions.

Senator LEVIN. That is all?

Mrs. SPECTOR. That is primarily what they have said.

Senator LEVIN. All right.

Mr. Saunders, a couple questions for you, and then I will turn to Senator Cohen. We have been unable to get any data at all about the extent to which NDI's are used. I understand that the OMB requested that DOD institute a formal information system to gather this data. Do you know why that information system has not been put together?

Mr. SAUNDERS. No, sir, I do not know why it has not been put together. I know that there are significant difficulties in counting the number of NDI's acquired. Any particular contract may have dozens of line items, some of which may be non-developmental items and some not. So it is difficult to count on a contract-by-contract basis.

The Army does count on a program-by-program basis.

Senator LEVIN. Well, have you answered the OMB? Have you told them you are not going to do it?

Mr. SAUNDERS. No, sir. As far as I know, we have not answered OMB at all.

Senator LEVIN. We thought it takes time for us to get answers. I mean, a year for the OMB to get an answer from the DOD seems like a long time. Would you answer that request to the OMB and would you get us a copy?

Mr. SAUNDERS. Yes, sir.

Senator LEVIN. The 1987 report of the DOD stated the Department was preparing a manual on the acquisition of NDI's. Has that manual been issued?

Mr. SAUNDERS. No, it has not.

Senator LEVIN. Do you know why?

Mr. SAUNDERS. Principally because I am the person working it; and I simply have not had the time to work on that because I have been handling other issues.

Senator LEVIN. Is there a timetable for that manual?

Mr. SAUNDERS. No, sir. There is not at this point.

Senator LEVIN. Have you asked for help?

Mr. SAUNDERS. Yes, sir.

Senator LEVIN. Have you gotten it?

Mr. SAUNDERS. Not yet, but—well, I take it back—yes, I have gotten help. We have doubled the size of the staff working on this issue.

Senator LEVIN. From one to two?

Mr. SAUNDERS. Yes, sir. [Laughter.]

Senator LEVIN. That is a 100-percent increase.

Mr. SAUNDERS. And in discussions with Mr. Katzen and Mr. Atwood last night, I was told that we are asking for a Presidential Executive Exchange Program person. So that would get us up to three.

I think, based on Mr. Atwood's interest in this issue, we can expect to see some further increase in what is going on.

Senator LEVIN. Has the FAR or the DFAR been revised to incorporate the Congressional preference for performance requirements? I emphasize for performance requirements—not for commercial items, but for performance requirements?

Mr. SAUNDERS. I am not sure about that. I do not believe that we have put anything in the FAR or DFAR that specifically says, "Use performance requirements."

Senator LEVIN. I do not think you have either. I think there is an NDI preference in there, but not a performance spec preference.

Do you disagree with that, Mrs. Spector?

Mrs. SPECTOR. The language I have says while there may be some mandatory design or performance requirements applied to a single phase or through the acquisition cycle, the citation of specification standards and related documents shall specify the results desired rather than how to design or how to manage. That is in the Defense supplement to the FAR.

Senator LEVIN. Our staff is going to talk with you about that after the hearing. One last comment about some of your testimony, Mr. Saunders, relative to the Competition in Contracting Act—I think Senator Cohen as the sponsor of that Act will go into some detail with you on it. And I will just simply say that I also noted that commentary, that after the prohibition was dropped from the Appropriations Bill in 1986, that now you are using the Competition in Contracting Act as the justification for not going commercial in a whole lot of areas.

Senator Cohen as the writer of that Act is the person to pursue this with you. I have to tell you, I will fully agree with his commentary on this, that it is not justification for going commercial. We think there is at least as much competition in that area, when you do go commercial, as when you write the design specifications.

I do not think there is any basis that you have for saying that a design spec will provide more competition than if you use a performance spec, and if you go commercial.

Senator Cohen.

Senator **Cohen**. I will just pick up on that, Mr. Saunders. It really caught my attention when, in page 3 of your statement, you indicated once one restriction was removed, the Competition in Contracting Act, with its heightened emphasis on full and open competition, kept DoD from returning to the practice of requiring commercial market acceptability as a condition of bidding.

That is just sheer nonsense; it is absolute nonsense, it was never the intent of the CICA Act. The purpose of CICA is an emphasis on competition, with some exemptions. When DoD, for example, has some unique products it needs, that are not commercially available; that is when you can go back to a sole-source contract.

And you say that CICA's keeping you from using the market acceptability as a pre-condition for bidding, there is just no basis in the history of that Act whatsoever for that interpretation.

Mr. **Saunders**. Sir, I know that that is not the intent of CICA, by any stretch. But the interpretation of our lawyers and our contracting officers, that the phraseology that says that all responsible bidders must be able to offer has kept us from including any sort of limitation, such as you must have a commercial marketplace for your item, as a limitation for making offers.

So, in order to make sure that we open the competition as broadly as possible, in compliance with CICA, we continue to use probably more detailed specifications than we should.

Senator **Cohen** [presiding]. Well, we will come back to this. I am going to declare a recess for about 15 minutes. We have a vote on. We will be right back.

[Brief recess.]

Senator **Cohen**. Mr. Saunders.

Mr. **Saunders**. Yes, sir?

Senator **Cohen**. Could we just pick up where we left off on CICA?

Mr. **Saunders**. Yes, sir.

Senator **Cohen**. I gather what you are saying is that, by virtue of the CICA Act, we now have manufacturers who might have no credibility as such, or acceptability in the marketplace—maybe even fly-by-nighters who want to buy into DoD contracts—and therefore, in order for you to prevent the fly-by-nighter or unreliable contractor to become part of the bidding process, you have to write restrictions into the bidding process that are more onerous; this has the effect of keeping out some qualified competitors—is that what you are telling me?

Mr. **Saunders**. Unfortunately, in a large measure, that is exactly what happens. We write specifications that are geared to try to protect us from companies who would sell less than quality merchandise to us. And we frequently include enough detail that we, then, force out of the competition some of the very best producers.

Senator **Cohen**. You mean to say, without those kind of restrictions or detail, you would not be able to exclude a contractor who simply wants to buy in when there is no reasonable basis to believe that he or it could complete that contract successfully?

Mr. **Saunders**. Yes, sir. Last night, as we were preparing Mr. Atwood for his testimony, he told a great story of a contractor to General Motors who was selling liquid cleaning fluid. Now, there were some other things that were going on—some illegal activities that were going on—but the liquid cleaning fluid that he was supplying to General Motors was water; and they were buying it.

Now, General Motors had the ability to say, simply, they will no longer buy that water.

Senator **Cohen**. DOD would not have the ability to say that?

Mr. **Saunders**. If the Department of Defense had issued a specification that said we wanted to buy liquid cleaning fluid, we would have had no basis on which to reject water. It is a liquid cleaning fluid.

Senator **Cohen**. Well, we will have to sit down and work this out. I cannot believe that we have worked ourselves into a situation where, on the one hand, we are trying to stimulate more competition to get away from a sole-source contracting, and then to the point where we are stifling competition because you are making it so restrictive that no one wants to bid.

Mr. **Saunders**. I believe it really probably is a problem of interpretation. As you said, I certainly do not believe that CICA was intended to do what it is, in some circles, being interpreted to do. But the term responsible bidder, in contracting, has a very specific meaning. And it means that anyone who meets all of the rules for being a responsible bidder must have an opportunity to bid. And that is the terminology that is used in the Competition in Contracting Act.

We have looked at some ways to include some new restrictions, some pre-qualifiers for contractors. And I think we may be able to do something more than what we are doing now.

Senator **Cohen**. Do not you have a whole system of pre-award inspections where you send out people to look at a firm to see who is employed, and what kind of capability they have? I know that goes on.

Mr. **Saunders**. Yes, sir; we do.

Senator **Cohen**. And doesn't that give you the kind of protection that—if you find somebody who has got a sham operation someone who is just starting up, does not have qualified people, and who has put in a bid which is unrealistically low, and has no hope of ever performing that contract—you mean to say you cannot exclude those people now?

Mr. **Saunders**. It gives us a certain measure of protection. Not all contracts have pre-award surveys performed. A large measure of contracting is done using small-purchase procedures that do not include a pre-award survey.

Senator **Cohen**. In your statement, you describe the elements of draft legislation that you intend to submit, along with the Office of Federal Procurement Policy. My understanding is that OFPP bill on commercial acquisitions would actually have a waiver for commercial purchases from any and all statutory and regulatory-mandated contract clauses. Is that correct?

Mrs. **Spector**. If I may take that question? It would say that only this law applies to commercial purchases. The intent would be to try to buy commercial items with the same rules that apply when commercial people buy from one another, and exempt the other requirements of law that are uniquely DoD, or uniquely Government.

Senator COHEN. Don't you think it would make more sense to identify exactly which statutory and regulatory requirements are impeding the NDI acquisition and when it would be necessary to waive it, rather than saying if it is commercial acquisition, we are going to waive all the requirements here? I mean, it seems to me, this is one of the problems I foresee in terms of going too far the other way, simply because it is a commercial acquisition; and now we are going to say that we are going to have a waiver for all of those statutory mandated regulatory clauses.

Why do we not identify those which are seen as impediments, and waive those, rather than waiving them all? It seems to me, we are going to get caught in the problem. And then, 5 years from now, when Senator Bingaman and Senator Levin, and I, might not be here—we are hoping we might not be here—come back and somebody is going to say, "You mean you waived all of those requirements simply because it is commercial acquisition?" Then you get caught, again.

Mrs. SPECTOR. Sir, that is how a lot of those requirements got there, because there was one problem; and we wrote a law so that it would never, ever, happen again. And by accretion, we now have about 50 different clauses that the law requires in commercial contracts that are burdensome. This law would give the flexibility to waive them when appropriate, which we do not have now. It would remedy that situation, as Boeing raised, where they were selling a product which was already manufactured, and they did not have the right clauses in their subcontracts; and the subcontractors had been lined up for 10 years, and would not accept the clauses—clauses that appear to be perfectly acceptable. But they just were not in those subcontracts. And contractors were unwilling to subsequently accept them.

I do not think we can conceive of every situation where we may need a waiver of a clause to buy a commercial, off-the-shelf item.

Senator COHEN. Well, Senator Levin asked you whether you were going to try to identify—sit down with contractors or the industry representatives—and identify those areas where they are an impediment to their participation. And I suppose you cannot do it and identify all of the clauses, but I think we ought to be a little more narrow in the focus. Otherwise, you are going to be criticized, at some future time, for waiving too many.

Mrs. SPECTOR. We can certainly consider that as the bill progresses out of OFPP.

Senator COHEN. In a March 23 letter to the Subcommittee, DOD cited a DOD supplement to the FAR as an example of how it has acted to encourage the use of non-development items. But the FAR itself still treats the purchase of NDI's as a permissible exception to the general rule of using military specs, instead of as requiring a preferred basis, which is what the NDI statute requires.

So the FAR says, you use military specs, but you can have an exception over here for NDI's. That is not what the legislation we passed requires. Ours requires that you have a preferred basis for NDI's, and not treat it as an exception.

Mrs. SPECTOR. We have changed the Defense supplement, to say that, pursuant to 10 USC 2325, it is the policy of the Department of Defense to fulfill requirements for items of supply through the acquisition of non-developmental items to the maximum practicable extent. That was issued last November 1st.

There is a preference. There is a definition of performance specifications—and a preference therefore. And that is in the DFAR, the Defense Supplement, since the law was passed, applicable to DOD.

Senator COHEN. That change was made, then?

Mrs. SPECTOR. It was made.

Senator COHEN. I was under the impression it had not been done.[1]

Mrs. SPECTOR. It has.

Mr. SAUNDERS. If I may comment, sir. The Federal Acquisition Regulation still has an order of precedence for selecting product descriptions; and it still shows a detailed specification as the number one item.

We plan to propose a change to the Federal Acquisition Regulation to reflect more nearly what we have in the Defense Supplement.

Senator COHEN. Industry officials, at our last hearing, said that no one, meaning the contract officer, has ever been publicly criticized for buying the lowest-priced product, if it met the minimal specifications, and that contracting officers tend to be too cautious and require too much data from contractors who produce commercial products.

It is like the situation, I suppose, we have in medicine today, where doctors tend to practice defensive medicine, in which they require more and more X-rays, more and more tests, in order to protect themselves against a future malpractice suit.

And the question I have is to what degree, in your judgment, are DOD's problems of unnecessary clauses, contract pricing data—can they be attributed to a lack of discretion given to the contracting officer? In other words, does he have sufficient guidance that gives him flexibility? Because the easiest thing to do is, when in doubt, just say no. This is the rule; and I do not care whether it is burdensome and whether it is even necessary. I am going to protect myself on this particular one, and just make you follow the book as it is written today.

Mrs. SPECTOR. If I may again?

Senator COHEN. Certainly.

Mrs. SPECTOR. We get a specification as contracting officers from a requiring activity. Anybody who meets that specification and is a responsible contractor—that is meets the specifications and is lowest-priced—we have great difficulty not selecting that contractor. We are very vulnerable to a protest if we do not select that contractor.

If we want to change the specification because we see something we like better, we have to provide everybody the opportunity to bid on that new requirement. We cannot just change the rules after the solicitation is out, and pick someone who offers something else, without allowing everybody to bid on it.

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[1] See footnote on p. 90.

So the general guidance to the contracting officer is, you pick the lowest price of the contractors who meet our requirements. Now, that is for very simple items. We certainly do not do that when we are buying a major weapons system. We have technical criteria and technical ratings, and we frequently do not pick the lowest-priced supplier in those circumstances.

However, in order to do that, we have to have discussions and go for a best and final offer. That is the way CICA reads; and that is the way GAO has interpreted it. So there are two different methods used, for simple items or for very complex items or professional services where you will get technical ratings playing a big role.

Senator COHEN. Also in your letter to the Subcommittee, the Department maintains that the primary regulations that cover the acquisition of major and non-major defense systems were revised in September of 1987 to require a consideration of NDI alternatives before starting new development programs.

I do not know which one of you to direct this to, but either one, take it. I guess the question I have is these regulations are sort of high-level publications that are only referred to when you have a new development program that is being considered—or is that the situation? And when do these revisions of September 1987, how do they translate into day-to-day operations as opposed to perhaps changing existing programs and not waiting for a new major program to come on line? How is the day-to-day application of those revisions taking place?

Mrs. SPECTOR. Those directives apply to major weapons system acquisitions, and all program managers have to follow them on major weapons systems. The DFAR's coverage that I referred to, which has several other provisions other than the ones that I read, would go out to all contracting people and would get disseminated that way. When we buying a major system the rules require one to look at what is already available. When we buy anything we look at what is already available, rather than build to a military specification.

Senator COHEN. Does it apply to on-going programs as well?

Mrs. SPECTOR. Anything that is not yet on contract, it would apply to. It would apply to any new orders; and we are doing, as you know, about 15 million of those a year. Any new order, this DFAR's coverage would apply to.

Senator COHEN. Mr. Saunders, I am not sure whether Senator Levin asked you this question—I think he perhaps did—but your letter states that the DOD directive—I think it is 5000.37—is currently being changed and expanded, and that this has been under review within DOD since March 1987.

So the question is, why the delay in publishing that directive? Is that because there was only one of you, and now, two of you?

Mr. SAUNDERS. Yes, sir. Coordinating a directive within the Department of Defense is a time-consuming process. However, last night in discussions with the Assistant Secretary, I got some new direction on that. And I believe that in a relatively short period of time, depending on when we get the Defense Science Board report issued, and whatever may come out of this Committee, that we can get some new direction issued.

Senator COHEN. Well, my staff reminds me that perhaps we have to be careful not to under-specify as well as over-specify in dealing with these issues. And I have a 15-page specification on oatmeal cookies that I shall read into the record.

Finished product: Type 1 oatmeal with chocolate chips. The cookie shall be well-baked. They shall be browned on the bottom surface and outer edges, but not appreciably browned on the top surface. They shall be wholly intact; free of checks or cracks. The weight of each cookie shall not be less than 13.7 grams. The diameter of each cookie, at its greatest dimension, shall be such as to enable easy placement of the cookie in the required lined can. However, the diameter, at its greatest dimension, shall not be less than 2⅝16 of 1 inch. The cookie shall be tender and crisp with an appetizing flavor, free of burnt or scorched flavor. Moisture content shall not be greater than 5 percent.

That is getting pretty specific, I would say; would not you?

Mr. SAUNDERS. Yes, sir.

Senator COHEN. Have we excluded any commercially accepted contractors with this? Is this designed to do that?

Mr. SAUNDERS. Sir, it was not designed to do that. I cannot say whether or not we have excluded commercial contractors. I know that we do have military specifications for many common food items which go into meals ready-to-eat, or operational rations. And because those have to remain shelf-stable, un-refrigerated, for up to 5 years, within a retort pouch, there are some unusual requirements for them.

I know also that we have some simplified specifications for many of the various kinds of cookies that we buy for base operations, and that we do have commercial suppliers for them. Keebler is a supplier for cookies. Certainly we will take a look at that one and see if we have shot ourselves in the foot yet again.

Senator COHEN. Does Mrs. Fields comply with this? [Laughter.]

Mr. SAUNDERS. I suspect that Mrs. Fields is a too high-quality cookie. [Laughter.]

Senator COHEN. That is all I have for now.

Senator Bingaman?

Senator BINGAMAN. Let me be sure, Mr. Saunders, that I understand the thrust of your testimony. It is that there was a period—and I am not sure of the exact time, you say early in the DOD's history—of trying to make greater use of commercial products, and you had this test program—the Defense Logistics Agency had a test program called Commercial Commodities Acquisition Program—when was that?

Mr. SAUNDERS. It began, I believe, in 1976, sir.

Senator BINGAMAN. 1976? And when did it terminate?

Mr. SAUNDERS. 1978.

Senator BINGAMAN. And it was just a test program?

Mr. SAUNDERS. Yes, sir.

Senator BINGAMAN. And it went for 2 years?

Mr. SAUNDERS. Yes, sir.

Senator BINGAMAN. And why did it end in 1978?

Mr. **Saunders**. We had discovered what we had intended to discover, that buying commercial products was indeed possible with very short purchase descriptions, and that we achieved some significant benefits by doing so.

Senator **Bingaman**. Well, if you discovered that in 1978, what was the result that accrued? I mean, you just ended the test program, and that was it?

Mr. **Saunders**. No, sir. We immediately began an institutionalization of the preparation of these very short purchase descriptions, and replacing military specifications with those or with non-Government standards, so that we could; in fact, infuse that across the entire Department of Defense.

Senator **Bingaman**. So that began in 1978?

Mr. **Saunders**. Yes, sir.

Senator **Bingaman**. And then, how long did that continue?

Mr. **Saunders**. That went until the restriction came about in 1983; and it was not completely brought to a halt by that restriction, but it was significantly modified.

Senator **Bingaman**. How broadly were you involved, or was the DOD engaged, in acquisition of commercial commodities as a result of that 5 years of trying to implement that test program on a wider scale?

Mr. **Saunders**. I am not sure of any specific numbers. I know that we created, along with the General Services Administration, a number of commercial item descriptions. I do not know how widespread that became.

Senator **Bingaman**. Is it possible at this date to go back and find those items that you had determined should be obtained commercially by the time the legislation, the Appropriations Act, got in your way in 1983?

Mr. **Saunders**. I do not know, sir; but I will certainly try.

Senator **Bingaman**. That would be useful, I think, if you could tell us here what items were commercially purchased at that time.

Mr. **Saunders**. Yes, sir.

[The information referred to follows:]

The following items were purchased under the Commercial Commodities Acquisition Program for 1976–78:

Aluminum sulphate, automotive gasoline, bath towels, bed sheets, black socks, box connector, boxer style drawers, brown sugar, calcium chloride, chlordiazepoxide, chain saw, clinical thermometers, cloth gloves, conduit, cotter pin, coupling, dental alloy, digital watch, door closers, double faucet, fireman's boots, fire extinguisher, food service equipment, fuel oil, fuses, granulated sugar,

Hex head screws, hot sauce, ice cream freezer, indoor thermometer, insulation, men's hankerchiefs, men's undershirts, microscope slides, microfiche viewer, photographic film, powdered sugar, protective shoes, radiator hose, rubber gloves, salad dressing, sodium chloride, solder, soy sauce, splice conductor, steak sauce, steam jacketed kettle, wall switches, waste drain, welding electrode, worcestershire sauce, x-ray film.

Additionally, DOD has prepared commercial items description for 2,227 different items.

Senator **Bingaman**. But your understanding was, first, the Appropriations Act stopped you from doing that; and then, by the time you were able to persuade Congress to relax that, the Competition in Contracting Act prohibited you from doing that? And so, unfortunately, we are now not as far along as we were when we started the test program in 1976?

Mr. **Saunders**. Yes, sir.

Senator **Bingaman**. And your understanding is that—you list several items here, towels, mustard, gloves—for those kinds of items, the reason why we could not buy commercially available towels; go through that once again for me?

Mr. **Saunders**. The difficulty we have today with buying commercially available towels is not being able to say to the world that we will only accept towels that have demonstrated commercial market acceptability. We find that we must specify, in a fair amount of detail, exactly what kind of towels we are talking about and some quality-assurance provisions to ensure that we do not wind up with unsuitable products.

Senator **Bingaman**. And you do not think you have enough discretion in the Competition in Contracting Act to reject bids that propose to sell you unsuitable products?

Mr. **Saunders**. Sir, I believe we do. But the lawyers who interpret it believe that we do not; that the clause that says any responsible bidder must be able to bid means that we have to open that up, not just to commercial——

Senator **Bingaman**. Yes, I understand that you have got to let a lot of people bid. I am not saying you can keep a lot of folks from bidding. But presumably, what you really are objecting to is not that a lot of irreputable types are bidding; you are objecting to the fact that if one of them bids and proposes to give you an inferior towel, you have got to buy it?

Mr. **Saunders**. Yes, sir.

Senator **Bingaman**. And your lawyers are telling you that you have to buy an inferior towel because of the Competition in Contracting Act?

Mr. **Saunders**. Not exclusively because of the Competition in Contracting Act; but if we do not establish a basis for rejecting an inferior towel somewhere in the solicitation, either the contract terms and conditions or the specification, then that is correct. We have to buy an inferior towel.

Senator **Bingaman**. And the legal advice that you get in the Department is that there is a necessary amendment to the Competition in Contracting Act so that you would have discretion to buy the quality of towel that you want?

Mr. **Saunders**. I am not sure that an amendment is necessary; perhaps a clarification is what we need.

Senator **Bingaman**. Well, it seems to me it would be either one or the other. If the law requires it—I mean, if your lawyers are telling you that the law prohibits you from doing what you were doing in 1976—then that means that the law has to be changed in order for you to do what you were doing in 1976. If the law does not prohibit it, then you could re-interpret the law within the Department of Defense; could you not?

Mr. **Saunders**. I do not sit at that kind of level, where I could re-interpret; but someone could, yes, sir.

Senator **Bingaman**. Well, who is the right person to do it?

Mr. **Saunders**. Perhaps at the Under Secretary level.

Senator **Bingaman**. So the Under Secretary could re-interpret CICA to permit what we are talking about here, in your opinion?

Mr. **Saunders**. In my opinion.

Senator **Bingaman**. But he has not done it.

Mr. **Saunders**. He has not been asked to do it.

Senator **Bingaman**. Who has not asked him to do it?

Mr. **Saunders**. He has not been asked. I have not asked him.

Senator **Bingaman**. Well, why have you not asked him? You are the guy in charge of getting this done.

Mr. **Saunders**. Yes, sir.

Senator **Bingaham**. Why do you not ask him to do that? Why do not you tell him, "We ought to be buying those commercial towels. Please re-interpret CICA to let me do it."

Mr. **Saunders**. We will put together a package, and get that up to him.

Senator **Bingaman**. It seems that there is a little bit of blame-shifting going on here; and I, as Senator Levin does, I concede that Congress is to blame for a lot of the problems in the procurement area. But it seems that we ought to be able to get together and agree that it was not Congress' intent to keep you from buying towels commercially and if that is the case, then if you think we need to amend CICA, then give us an amendment. If you do not, then re-interpret CICA to allow you to do what everybody wants to have happen.

If there is a problem with that, I need it pointed out to me.

Mr. **Saunders**. No, sir. That is clear.

Senator **Bingaman**. Mrs. Spector, let me ask you, on the legislation that you refer to in your testimony that you have been working on with the Office of Federal Procurement Policy. I guess that has been going on for some time now, that legislation.

I have some frustration with the situation we have here. You point out in your testimony that much of the problem is in the statutes that we have written; and we can take exception on specific ones. But granted, that much of the problem may be in the statutes, how do we get the proposed changes in those statutes from DOD and from OFPP, or whoever has got them.

I understand that this has been working its way through the system, this legislation, for at least 2 years. And we do not seem to be able to get it, to make the changes in the law. We are going to mark up a Defense bill in another 6 weeks; and it would be great to have an idea as to what we ought to change, if there are some things.

Mrs. **Spector**. I would suggest you address that question to OMB.

Senator **Bingaman**. That is where the problem is, OMB?

Mrs. **Spector**. Our proposal has been there, as you suggest, for almost 2 years; and we are very eager to see it forwarded to the Congress.

Senator **Bingaman**. Well, we will contact them and try to get it done. But as I say, I just think that to the extent that your criticism may be valid, that Congress needs to change some things in order to let you do your job, Congress needs the recommendations that folks like yourself, who work in the system, have been able to come up with. And I think that would be a great help, if we could get that, because this problem has not diminished in the last 2 years; and it is certainly not going to go away, absent some of those changes.

Let me ask, in general—I have had some real concern and real questions as to how the making of acquisition policy and regulations works within DOD. If you adopt a regulation—for example, you have got a general sort of preference for non-developmental items being bought commercially—does each service then have its regulations that interpret that, or how does this work? I mean, we seem to have such—the point that Senator Levin was getting into—we have got such inconsistency in the procedures that are followed, not just in this area, but in an awful lot of areas of acquisition, between the services and the Defense Logistics Agency and various others. How do we get to a more uniform system?

Mrs. SPECTOR. By and large, by issuing more regulations to tie things down even tighter.

Senator BINGAMAN. At the Department level?

Mrs. SPECTOR. At the Department level. But some of the inconsistency is not necessarily negative. It leaves flexibility in this system to accommodate different circumstances. It is not all bad.

My concern with just the accusation of inconsistency is, the commercial people that I have talked to have not pinned down which aspects of that have a deleterious effect on their bidding. There are valid differences among the Services and among procurements.

The one consistent problem they have raised is cost and pricing data; and we are setting about writing a FAR change to correct that problem, to make it much easier to qualify as a commercial source with substantial commercial business. We are proposing making a very major FAR change to accommodate that.

Senator BINGAMAN. When you do that FAR change, is there still a danger that we will have inconsistent applications of that across the services, or you do not consider it a danger?

Mrs. SPECTOR. Yes, well, there is a danger. There is always that danger. The only way you can preclude any inconsistency is by saying you always must or you never can waive this; and we do that in certain areas. Cost principles is an area the Services cannot waive without coming to a very high level, for example.

In many areas, we give the Services the flexibility to do what is right; and that also gives them the flexibility to do what is wrong.

Senator BINGAMAN. Well, I understand. And I favor giving them flexibility. I am just wondering about giving them authority to issue other regulations. Is that necessary? Is it unreasonable to think that you could have a consistent set of regulations covering one of these subjects, adopted at the DOD level, and those would give enough flexibility to everybody that they could go ahead and implement them appropriately?

Mrs. SPECTOR. Senator Bingaman, they do, by and large. Our IG looked at the Service supplements and determined there were only about 20 items that possibly belonged at a higher level or were inconsistent; and we have corrected all of those.

Senator BINGAMAN. In this area, or in general?

Mrs. SPECTOR. No, in all.

Senator BINGAMAN. Across acquisition?

Mrs. SPECTOR. Across acquisition.

Senator BINGAMAN. Is that right?

Mrs. SPECTOR. Yes. The Service supplements to the FAR by and large, are procedural. They say things like whom you send your business clearance memorandum to. They certainly are not allowed to negate anything that is in the FAR or the DFAR's. They can supplement for unique circumstances; and they do, for instance, in the area of ship-building, which is Navy-unique.

But by and large, they do not conflict. I take action any time it is brought to my attention that there is a service clause or a regulation that conflicts with the FAR.

Senator **Bingaman**. Now, the IG did an analysis of this?

Mrs. **Spector**. Yes, sir. Yes, they did.

Senator **Bingaman**. And when was that, fairly recently?

Mrs. **Spector**. About 2 years ago, as I recall.

Senator **Bingaman**. Could we get a copy of that analysis?

Mrs. **Spector**. Certainly.[1]

Senator **Bingaman**. That would be very useful.

Mrs. **Spector**. And we have made every correction that they recommended, or they are in the process of being made.

Senator **Bingaman**. That would be very useful.

I think that is all I had to ask. Thank you, Mr. Chairman.

Senator **Levin** [presiding]. Thank you very much, Senator Bingaman.

Mr. Saunders, on the point that Senator Bingaman made about the CICA law and your role, and what you are going to be doing, would you provide the Subcommittee staff with a copy of that legal opinion that you made reference to, that said that CICA precludes reliance on commercial item acceptability?

Mr. **Saunders**. I will endeavor to do that. I am not sure exactly where that legal opinion came from; but I will make every attempt to get it.[2]

Senator **Levin**. I am not sure what you mean, where it came from. It came from your lawyer, I presume; did it not?

Mr. **Saunders**. It occurred before I became deeply involved in this program. I think it came from the OSD General Counsel's office, or one of the Services or Defense Agency Counsel. It could very easily have come from the DLA counsel. But I will make every attempt to get it.

Senator **Levin**. Do you know where that opinion came from?

Mrs. **Spector**. No, sir. What may be referred to—and I am really not familiar with this at all—there has been a concern with excluding small businesses that do not have the commercial market acceptability. That has been a continuing concern, excluding those sorts of businesses.

Senator **Levin**. I am not talking about vague concerns. I am talking about specific opinions.

Mrs. **Spector**. No, sir. I do not know of it.

Senator **Levin**. You made reference to a specific opinion; and it has got to exist somewhere. So we will count on you to provide that to the Committee.

Mrs. Spector, I understand that you have provided us with a November 1988 amendment to the DOD FAR supplement, which does incorporate the preference for performance specs. Apparently, in the last hour or so, you have made that available to us. We appreciate that; which means that what I said before was in error.

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[1] See p. 389.

[2] See p. 398 for a paper prepared by the Procurement Directorate of the Defense Logistics Agency with the assistance of their Counsel which addresses DLA's view as to the effect of 10 U.S.C. 2305(a)(1), Competition in Contracting Act, on the acquisition of Commercial products.

It was not in our version of the DFAR. And the people that our staff contacted about this were not aware of the change; and that is the reason why I said what I did.

Mrs. SPECTOR. I understand.

Senator LEVIN. Yes, but you had better also notify the DoD people.

Mrs. SPECTOR. I do not know whom you contacted.

Senator LEVIN. We will let you know who we contacted, because somebody who should know does not know, beside me. We will let you know who that was.[1] But in any event, you were correct in saying it had been incorporated.

Mrs. SPECTOR. Yes, sir.

Senator LEVIN. And I was in error. But there are a lot of other people under that same misapprehension inside the Department of Defense.

Mrs. Spector, in your prepared testimony, you state that many of the contract provisions that are troubling to contractors are required by statute, and I do not disagree with that. Your testimony also refers to a list which was provided by Mr. Pinick of Boeing at our last hearing, a list of contract clauses that are required to be flowed down to subcontractors. And you state that all 19 of these clauses are required by statute—in your prepared testimony—and that, I believe, is erroneous.

While all of the clauses have a statutory basis, it is simply not true that they are required by statute to be flowed down to the subcontractors. And I want to start down Mr. Pinick's list with you.

At the beginning of his list, the statutory provision on direct subcontractor sales to the Government provides that, "The contractor will not engage in prohibited activity."

So the statute makes reference to the contractor. But the regulatory implementation of that provision states that the contractor agrees to incorporate the substance of this clause, including flowdown, in all subcontracts under this contract.

Mrs. SPECTOR. You are right.

Senator LEVIN. So when you point to a statutory basis, the statute specifically says the contractor will not engage.

Mrs. SPECTOR. You are correct, sir.

Senator LEVIN. Now, the second item on Mr. Pinick's list is the Anti-Kickback Act. The Act refers to duties of prime contractors, in quotes. But the regulation requires flow-down to subcontractors at all tiers.

In fact, I was the author of the Anti-Kickback Act. And I specifically wrote to the FAR's Secretariat to complain that the regulatory implementation was too broad and too burdensome.

The third item on Mr. Pinick's list is the Defense Priorities in Allocations System. Here, the statute simply authorizes—I emphasize authorizes the President—to place a priority on Defense contracts where he deems it appropriate. But the regulatory implementation places such a priority in all DOD contracts over $500, and requires a flow-down to all subcontractors and vendors. It is an extremely burdensome thing. There are contractors who just simply are not going to replace their routine orders to their commercial customers, and put the Government business first. They are not going to do it; and it is not always required that they do it.

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[1] The Department of Defense provided a copy of the relevant DFARS provision as an attachment to its April 21, 1989 letter to the Subcommittee. The copy of the regulation provided by the Department of Defense did not include, or reference, the November 1988 revision to the regulation.

Under our law, it authorizes the President to do it where he deems it appropriate. So that is very different from having an automatic flow-down of a requirement to put Defense business ahead of private commercial business. And yet, that has been flowed down.

So would you agree that at least with regard to those three provisions, that it is the regulations, and not the statutes, that are the problem?

Mrs. SPECTOR. On the subcontract level, you are correct.

Senator LEVIN. And will you take action to ensure that those regulations are revised, and that the regulations incorporate appropriate exemptions for commercial manufacture?

Mrs. SPECTOR. At the subcontract level, sir?

Senator LEVIN. Yes.

Mrs. SPECTOR. At the prime level, we obviously cannot.

Senator LEVIN. Yes, on the flow-down issue.

Mrs. SPECTOR. We will look into making those changes.

Senator LEVIN. Well, will you let us know what you do on that?

Mrs. SPECTOR. Yes, certainly.[1]

Senator LEVIN. One of the contract requirements which our witnesses at the last hearing identified as an impediment to contracting with the Department of Defense was the requirement for cost or pricing data. And your testimony indicates that you are now considering regulatory changes that would broaden the commercial exemption to this requirement, and give contracting officers greater latitude in determining whether a product is sold in substantial quantities to the general public.

As I understand it, this draft was prepared within the last month or 2. However, the problem that it seeks to address was identified 2 years ago when DOD submitted its report to the Congress on the implementation of the NDI provision.

And my question is why has it taken so long to put together a proposal on that issue?

Mrs. SPECTOR. We have had several discussions with the industry people since that time; and it does take awhile to evolve a regulation that is appropriate. We have been working with the industry people to do just that; to pinpoint where the problem was; what needed to be changed, working within our system, to come up with regulatory solutions. It sometimes does take that long.

Senator LEVIN. Two years?

Mrs. SPECTOR. Sometimes.

Senator LEVIN. Has the industry been dragging their feet? I would think they are pretty anxious to get this done.

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[1] Mrs. Spector has informed the Subcommittee that DOD has initiated an effort to review all of our procurement regulations and contract clauses to streamline and simplify the subcontracts as part of this effort.

Mrs. SPECTOR. Senator Levin, the industry, to some extent, was giving us generalizations on the problem. We could not determine if it was contracting officers inappropriately doing things that the regulations would not necessarily condone, or whether regulatory change was necessarily needed.

Senator LEVIN. I think both.

Mrs. SPECTOR. It is both. And we have concluded the same thing.

Senator LEVIN. I find the industry very specific. I mean, we went through specific examples at the last hearing; that was one of the points of it. And so, I do not think there is a vagueness here on the part of industry.

And what I would like you to do—and I think this is in line with what my discussion was with Mr. Atwood this morning—what I would like you to do is to get together with my staff and with representatives of industry, set aside some time; go through some examples together. But I would like our Subcommittee staff, you and the industry people—and we will suggest to you who they will be, and you can make many modifications before they are invited—to go through these problems together. It is going to take a chunk of time to do that. Are you willing to do that?

Mrs. SPECTOR. Absolutely.

Senator LEVIN. It is one way to get very specific, is to have that kind of a meeting with specific contract in front.

Mrs. SPECTOR. I will be glad to do it.

Senator LEVIN. And we can go through them. The industry witnesses at the earlier hearing raised a number of very specific problems, as I have stated, on the way that commercial pricing exemptions—the cost of pricing data requirements—have been applied to the Department of Defense.

And these problems included the application of the exemption to: one, large Government buys that skew the percentage of products sold to the general public; two, to newly developed products intended for sale to the general public, but without a sales history; three, to old commercial products that are no longer sold in the commercial world; and four, to spare parts for commercial products. So those four specific areas were identified by them.

Do you agree that the application of the exemption to these type of products has been a problem?

Mrs. SPECTOR. Yes, I believe it has.

Senator LEVIN. And are these issues covered by the revised regulation that you are working on?

Mrs. SPECTOR. Yes, sir; they are.

Senator LEVIN. All four of those issues?

Mrs. SPECTOR. Yes, sir; they are.

Senator LEVIN. Each of those four problems that I just listed was specifically identified as impediments to the procurement of NDIs, and the draft of the DOD 1987 report that I have referred to; that the final version of the report deleted that information.

Do you know why the reference to those specific problems was deleted from that 1987 report?

Mrs. SPECTOR. No.

Senator LEVIN. Could you try to go back and reconstruct that? I think if we go back into the history, we may learn something there that can help us in taking this step a little quicker now.

Mrs. **Spector**. Some of the concerns with the report were generalizations without targeting or pinpointing what was the problem, why were people doing this.

Senator **Levin**. It is not the why. I mean, you have acknowledged something which is pretty clear, that those four areas are problems. I mean, you just acknowledged that. They were identified as problems in that report—just what you said—in a draft. And yet, when it came to the final version, it was watered down. And if we can find out what are the forces in the Defense Department which would cause the watering down of four things which are real—which you acknowledge are real—if we can find out why that was watered down 2 years ago, it may help us in trying to overcome these impediments now.

Did you review that report, by the way? Were you involved in drafting or reviewing, or preparing, that report?

Mrs. **Spector**. Yes, I read the report. I was not involved in drafting it.

Senator **Levin**. Did you comment on the draft?

Mrs. **Spector**. I believe we did give some comments on the draft.

Senator **Levin**. Do you remember objecting to those specified areas, or commenting on those areas?

Mrs. **Spector**. We had some concerns with there being generalizations. For instance, there was an attack on CICA that was somewhat general that we did not agree with. There were some attacks in areas that we felt were not sufficiently specific. And I know we requested that those be deleted.

Senator **Levin**. Let me read you the draft report provisions here.

Item 1: Sales of product to the private sector originally meant percentage requirements to be exempt from submission. Large Government buys skew the percentage to the extent that subsequent buys no longer qualify for the exemption, even though the product is still being sold in the same substantial quantities to the general public.

I mean, that sounds just like what I was saying today, and what you agreed to. And yet, that was deleted.

Mrs. **Spector**. Yes. I do not know why.

Senator **Levin**. Another one: A newly developed product, clearly intended for sale to the general public, but without a history of substantial sales to the general public. That is the language from this draft report; and that is what I read to you. And that is what you said is a problem.

Mrs. **Spector**. Yes, it is. I do not know why those were deleted.

Senator **Levin**. As Casey Stengel would have said, this is deja vu all over again.

And hopefully, this will be the last deja vu on it.

Mrs. **Spector**. I think the coverage that we are proposing would certainly make accommodations for those problems.

Senator **Levin**. On the consistency issue again, the way that I would like to leave that with you is that you, industry, Subcommittee staff, will meet.

Mrs. **Spector**. Yes, sir; be glad to.

Senator **Levin**. And we will organize that. We will make sure it is set up in a way to be most constructive. We will ask industry for some suggested representatives that can present specific contracts and examples. We will let you know who it is. You may like some other people there. We would be happy to consider that, so we can really put together something. It is going to take time.

Mrs. **Spector**. Be glad to do it, though.

Senator **Levin**. But we have to work from the specific to the general, as well as to the specific from the general.

Testimony at the last hearing indicated that DOD does not yet accept GSA's determination about products being sold in substantial quantities to the public. And as a result, Hewlett Packard testified that it files more than 1,000 requests for exemption with DOD every year for products that the GSA has already placed on its multiple awards schedule.

Could you square the Department's position that it does not recompete products on GSA schedules with the Hewlett Packard testimony?

Mrs. **Spector**. We were competing products on some of the GSA schedules because occasionally we felt that the schedules did not contemplate the size of the DOD buy. We have since changed that FAR coverage; and the new coverage would say regarding GSA schedules that if there has been a determination within the past year that an item is a commercial item—that we would accept that determination. And that is clarified in the new FAR coverage.

I might also say something that would help——

Senator **Levin**. Is that something that Hewlett Packard does not know about?

Mrs. **Spector**. Hewlett Packard does not officially know about it yet. We have worked with some Hewlett Packard people on drafting this new coverage; so they are somewhat familiar with the fact that we are considering it in our new coverage. But officially——

Senator **Levin**. It has not been done yet; has it?

Mrs. **Spector**. No, sir, it has not been done yet. We did put out guidance on that point earlier.

Senator **Levin**. Where does that go now? Does that go to the DAR Council?

Mrs. **Spector**. Yes. It would go to the DAR Council first; and since it is FAR coverage, it would then go to the FAR Council for their concurrence as well.

Senator **Levin**. The FAR Council's name——

Mrs. **Spector**. Or rather—excuse me—the civilian agency council.

Senator **Levin**. The FAR Council's name, I think, has some symbolic significance. It seems far away in time, sometimes. [Laughter.]

Mrs. **Spector**. Usually.

Senator **Levin**. I am wondering, can you give us a timetable? Here we now have a situation—I mean, just think about it—you have got a manufacturer, applying for 1,000 exemptions per year for something that has already been approved by one Government agency. It costs money. I mean, we are paying for this. It is just a bunch of duplication.

You are now saying, "Okay, we will accept the GSA. If it has been certified in the last year, we will buy it." That is what you are proposing to DAR and to FAR, and to a few others. Now, is this a 6-month wait, a year wait, a 2-year wait, assuming it is approved?

Mrs. SPECTOR. We have put out guidance like that directly; and we can do so again. The FAR process is very, very slow; and again, some of the process is in law.

Senator LEVIN. But wait. Hold up.

Mrs. SPECTOR. We have comment periods.

Senator LEVIN. Hold up a minute. Hold up a minute. You say, you can put out guidance directly?

Mrs. SPECTOR. We can on some of these areas, yes.

Senator LEVIN. In other words, you can do that right now?

Mrs. SPECTOR. Yes, in certain specific areas.

Senator LEVIN. How about that area?

Mrs. SPECTOR. We may well be able to do it in that area. The problem becomes that we are not supposed to put out anything affecting the public without a public comment period. So we have to be sure that what we are putting out is purely internal guidance. In this case, I think it would be; and we can put out something fairly quickly for that specific area.

Senator LEVIN. That is all I am asking you about, was that specific one.

Mrs. SPECTOR. We also, sir, contend with our IG's criticism that we are waiving cost and pricing data when we ought not be waiving it. And we have a recent IG report that says exactly that; that we should tighten up on our regulations on cost and pricing data.

Senator LEVIN. I am just talking about one specific area.

Mrs. SPECTOR. I understand.

Senator LEVIN. In that one, narrow area, has the IG ever said you should not accept the GSA exemption?

Mrs. SPECTOR. Well, we have to do at least a price analysis to show that the quantities that GSA contemplated are the same quantities, terms and conditions that we are contemplating.

In addition, if we make any changes at all, we are supposed to do a cost analysis on those changes.

Senator LEVIN. On just that one issue of whether they are sold in substantial quantities to the public, just on that question?

Mrs. SPECTOR. On that determination, I do not believe——

Senator LEVIN. Has the IG ever said that you should not take the GSA's determination for that as presumption for your own use?

Mrs. SPECTOR. I do not know. Then again, there has been the allegation that our quantities are so different from what is contemplated on the GSA schedule that we need to do more work to do price analysis.

Senator LEVIN. It is their determination that the products are sold in substantial quantities to the public?

Mrs. SPECTOR. Again, our quantities sometimes skew even that, because our quantities are not considered sales to the public. The new FAR coverage would say that anything sold competitively or to a GSA schedule would now be included as a commercial sale rather than as a sale to the Government. That has been a very major issue, that our quantities do skew the percent of commercial sales.

Senator LEVIN. Would you let us know, for the record, whether or not you are going to be providing that guidance?

Mrs. SPECTOR. Yes.

Senator LEVIN. And if not, why not?

Mrs. **Spector**. Yes.

Senator **Levin**. There is a lot of follow-up here. We do not have another hearing scheduled; but there is a tremendous amount of follow-up. And we are going to stick with it. We hope you are going to stick with it, because 2 years from now, we do not want to go through another set of two hearings with the same subjects, and probably the same people.

We would really like to wrap up something in 6 months in this area—the changes we have talked about today, the meetings. Six months from now, what I would like is our Subcommittee staff to go through the items that we have talked about and say, here are the 10 items—5, whatever it is—these are the problems that they identify that you have frequently acknowledged here this morning, that our industry people have pointed to. This is what is going to be done, on what timetable, or this is why nothing can be done.

It is a tall order. There is a tremendous momentum. There is a way of doing things there that is very hard to change. And I think the best way to describe it is that we require exemptions and exceptions to be identified, in order to go commercial, rather than vice-versa, or rather than give them equal presumption.

It is a whole atmosphere that I think has to be changed. Directions have to get down to the bowels of the buying system on changing things. But there is a lot of money involved here. There is a lot of waste; a lot of duplication; a lot of frustration; a tremendous amount of frustration which leads to hostility at times; but at a minimum, frustration that I really believe we can avoid.

If you need some additional help, you ought to ask for it. Six months from now, I will be asking the Subcommittee staff, "Did Mr. Saunders ask for help? Did he get help?" If this is your responsibility—you may not be at the top of this organization chart—but you are the one that is going to have to be the squeaking wheel on this thing, at least at your level; otherwise, this frustration is going to continue, and the waste is going to continue.

We are grateful for your testimony, for your appearance here today. And we will be getting back with you to work this out.

Mr. **Saunders**. Thank you.

Senator **Levin**. Thank you. This hearing stands adjourned.

[Whereupon, at 12:15 p.m., the Subcommittee was adjourned, subject to the call of the Chair.]

APPENDIX

TESTIMONY

OF

ROBERT ROSSOW III

OF

MIDLAND BRAKE, INC.
Owosso, Michigan

Given Before The
SUBCOMMITTEE ON OVERSIGHT OF GOVERNMENT MANAGEMENT
COMMITTEE ON GOVERNMENTAL AFFAIRS
UNITED STATES SENATE
WASHINGTON, D.C.

16 MAY 1989

1. INTRODUCTION

Midland Brake, Inc., is a wholly-owned subsidiary of Echlin, Inc., of Branford, Connecticut. Echlin, currently 282 on the Fortune 500 list with about $1.3 billion in sales, is a major manufacturer of automotive brake and electrical system components.

In August 1982 Echlin purchased Midland Brake from the now defunct Midland-Ross Corporation. At that time Echlin had virtually no government sales due to deliberate corporate policy. However the Midland purchase brought Echlin firmly into the government market and Midland's government sales organization was given the responsibility for the marketing and sales of other Echlin division products to the government.

Midland is headquartered in Owosso, Michigan and has manufacturing locations throughout the nation. Our principal customers include all major domestic vehicle and construction equipment manufacturers. We also enjoy extensive aftermarket sales through our distribution system. Our military customers include AM General, BMY, General Motors, Hercules Engines, Lorel, Oshkosh and Teledyne as well as the Tank-Automotive Command and Defense Logistics Agency among others.

Currently less than one percent of Echlin's annual sales are government related. However that figure belies our place in the market due to the relative low cost of brake system components. There is hardly a tactical vehicle in the motor pool from the Jeep to the 10-ton HEMTT which does not use our components.

We make the brake systems on all the new crash trucks and Midgetman's Hard Mobile Launcher. We are on all the prototypes for the Family of Medium Tactical Vehicles as well as most of those for the Palletized Loading System and Heavy Equipment Transporter.

Although some might consider our position enviable, it is risky for a firm as commercial as Midland for both internal and external reasons. Except when crises arise, the market receives limited attention due to its small relative size. While the market is recognized as having special rules and problems commercially oriented managers find the complexities of government contracting difficult to comprehend. They do not understand why a government operation requires the level of administrative overhead it does. It is hard to explain to anyone with a reasonably logical and practical mind why problems which can be resolved with a phone call or two in a commercial environment take months if not years to clear up.

Government business is not fun. Nonetheless Midland provides its government sales organization a remarkable amount of support given the overall level of sales. Other Echlin units have considerable undeveloped potential in the defense market. The question is do we want it? Do we even want the business we have? When one percent of your business seems to create 80% of your problems, you wonder.

II. PROBLEM AREAS

The external problems a commercial vendor faces include specifications, technical data rights, cost and pricing data, contract management and social and compliance program requirements. Moreover, these problems vary depending on whether one is dealing with a prime contract for repair parts from a government agency or a subcontract from an original equipment manufacturer.

III. SPECIFICATIONS

Specification problems for a commercial manufacturer engaged in government contracting include design versus performance specifications, multiple simultaneous specification levels, and overspecification.

a. Design Versus Performance

Consumable repair parts, meaning those discarded rather than repaired, can provide the government an excellent opportunity to take advantage of commercially available products. Hydraulic brake system components provide a good example. In addition to Midland four other major manufactures produce competing products: Bendix, Delco, EIS, and Wagner. All five manufactures's parts are identical for all practical purposes. While minor variations exist, none are significant with respect to form, fit and function. Since all five companies compete for the same spot on the same vehicle, they cannot be significantly different.

Unfortunately, the Department of Defense procures hydraulic brake parts by means of design specifications. Some even go to the extreme of specifying the direction of rotation of the helix of a spring. Many of these date back to the late 1940's and early 1950's and even the original manufacturer no longer makes the item to the drawings.

When Echlin purchased Midland, it was obvious to me that many opportunities existed for Echlin. It was also obvious that most Echlin products, while similar, were not identical to the technical drawing packages (TDP). Commercially this is irrelevant as long as the product meets the basic requirements of form, fit, and function. With government contracting such is not the case. I knew that to be successful selling our products to the government I had to get the specifications changed from design to performance. Thus began a five year campaign.

Midland bid on and won several hydraulic repair parts solicitations. Following awards we submitted requests for waivers each of which proved a lengthy and frustrating experience. Throughout the process we continually asserted that these components should be procured through performance specifications. Although the engineers agreed in principle, nothing occurred. The passage of the Competition in Contracting Act (PL 98-369) and The Small Business and Federal Procurement Competition Enhancement Act of 1984 (PL 98-577) gave me the moral high ground but little else. It was clear that dealing with engineers and buyers was not going to be a successful axis of advance.

In May 1985 I wrote General Flynn, then the U.S. Army Tank-Automotive Command's (TACOM) Deputy Commander for Procurement and Readiness, proposing an industry-government conference on brake system repair parts specifications and procurement which the General endorsed. I also informed General Garrison of the Defense Construction Supply Center (DCSC) of the meeting since DCSC purchases many items for TACOM. The meeting was held November 13, 1985 at which it was decided to move toward performance specifications based on industry standards.

In the meantime the struggle continued. DCSC began to issue solicitations for these parts as competitive proposals which allowed the submission of alternate offers but the need for engineering approvals remained. The process was laborious and time consuming and one had no guarantee that because a waiver was approved on one contract it would be approved on the next. Since the departure of General Garrison DCSC has slipped back into its old ways and tends to treat the Requests for Proposal as if they were Invitations for Bids and will not consider technical variation.

In one case Midland, after having provided more than 180,000 wheel cylinders without a quality deficiency report of which we are aware, was informed by DCSC our product was technically unacceptable. A similar scenario occurred with a master cylinder solicitation. In both cases Midland was clearly the low bidder. Needless to say both prompted protests, the first to the head of agency, the other to the General Accounting Office. Both were denied.

In mid 1988 some of the revised specifications began to appear. Unfortunately industry had not been consulted during their drafting so they varied considerably from standard SAE practices and some were poorly worded in addition. This precipitated another letter to General Flynn, now TACOM commander, suggesting another government-industry meeting on the issues. Once again the General concurred.

The meeting was held January 31-February 1, 1989. Prior to the meeting TACOM engineering distributed their drawings and specifications and solicited industry comments. The meeting was remarkably frank, forthright, and productive. The results are a set of specifications which are realistic and address the concerns of both industry and the military. Its success was due in a large part to its Chair, Mr. Alex Sinclair, TACOM's Chief of the Tactical Vehicles Division of the Directorate of Systems Engineering. Mr. Sinclair is a practical gentleman of considerable experience and most importantly, unafraid of making decisions. Since then the specification revisions based on the meeting have been circulated. Everything appears as agreed and they will be released shortly.

But the war is not over. Even as I was preparing this testimony a solicitation was released for one of the covered master cylinders using the old specifications. When I talked to General Flynn following the meeting he admonished me to "keep them honest". So I picked up my pen and filed my protest.

Although the preceding may seem a success story, and in many respects it is, it is nonetheless a limited success. The reason is that these performance specifications and SAE standards apply to only ten of the most visible brake system components on the largest vehicle fleets. Hundreds of parts on the "cats and dogs" continue to be procured by design specifications. Whereas the ten covered parts are purchased in quantity others are not and few would tool up for half a dozen master cylinders. However, in many cases functional equivalents are probably readily available at reasonable cost.

Why was I successful? Part was perseverance reinforced by a sense of civil responsibility. Part was knowledge both of the item itself and its end application. As a reserve component Cavalry officer I have "owned" many of the vehicles for which Midland makes parts and am very familiar with organizational maintenance practices. Part was a favorable legislative environment created by the Competition in Contracting Act and related legislation. Part was favorable command attention. But probably the most important part was that the quality standards I sought were clearly superior. That is hard to fight.

After the January meeting one of my competitors came up and thanked me for getting his firm back in the business. He said they had attempted unsuccessfully to do what I had done and as a result had withdrawn from the market, something I had noticed because they were conspicuous by their absence. Their return does not bother me; I will meet them in the bid room. But I have to say had the meeting not gone the way it did we would have also withdrawn from that segment of the market.

b. Multiple Simultaneous Specification Levels

Another sort of specification problem occurs when one is obliged to provide the same part in slightly different forms on simultaneous contracts. This situation occurs in the following manner. An original equipment manufacturer (OEM) receives a contract to deliver vehicles built to a technical drawing package (TDP) which contain design specifications of a specific revision level. The OEM then orders parts from his vendors to his particular TDP. The years pass and the vendor continues to deliver. Then the vendor receives a repair parts contract for one of the parts but to an updated technical drawing package. The vendor now has a production control nightmare unless he can persuade one of his customers to make a change. Experience suggests both will resist. However, had the part been fielded to a performance specification this situation would not have occurred.

c. Overspecification

Overspecification is yet another problem area and packaging provides as good an example as any. I understand that the basic packaging standard, MIL-STD-2073, is really a decent specification which has provisions for everything from commercial pack to extreme levels of protection. Unfortunately no one seems to have read beyond the extreme levels. The result is the absurdity of packaging a five cent o-ring in two dollars worth of box.

Another example is foam-in-place packaging. This packaging method is quite expensive; for hydraulic brake boosters it costs roughly ten dollars more than heavy duty waterproof boxing. It also doubles the cube which increases both shipping and storage costs. Although the intent is to maximize protection of the parts prior to their use, things often do not work out that way. The reason is that a unit's parts van has very limited storage space. As a result when one of these bulky boxes arrives the part is frequently removed from the box and stored without protection. So much for the investment in packaging.

This overspecification creates other opportunity costs. Recently a repair part solicitation which had a value of roughly $200,000 was cancelled for lack of funds. At the same time a contract was awarded for another part which called for foam in place packaging. The incremental cost of that packaging? Roughly $400,000. Need I say more.

I have challenged contracting officers on this issue. Although they acknowledge that the requirements seem silly and that they have the authority to override the requirements, they will not because "the experts are the experts and who am I to question them".

IV. TECHNICAL DATA RIGHTS

The commercial automotive market is highly competitive. As a result firms participating in the market are reluctant to give out detailed engineering data on their products especially when those products were developed entirely at private expense. Nonetheless the government exerts considerable pressure on its vendors to provide such data for competitive reprocurement.

One learns in Management 101 that the basic responsibility of management is to maximize the value of the firm. This is seldom accomplished by giving away proprietary data and trade secrets. The matter really reduces itself to one of specifications. If the government really wishes to take advantage of competitive commercial products, then those items should be defined by performance specifications.

V. COST AND PRICING DATA

a. General

Most firms regard cost and pricing data as highly confidential and strongly resist divulging it to anyone for any reason. This includes Midland. On the other hand we recognize the government's concern that the public receives due value. Being a commercial firm with modest government sales Midland does not keep its books in accordance with either the Cost Accounting Standards or Part 31 of the Federal Acquisition Regulations (FAR). Moreover in most cases we can easily justify an exemption from furnishing cost and pricing data based on commerciality. Nonetheless preparing a request for exemption is only slightly less onerous and time consuming than submitting full cost and pricing data and still releases sensitive information outside the company. We particularly dislike providing such information to a prime contractor as this can complicate commercial relations with that firm.

b. Government Purchasing Practices

Although it is frequently possible to claim an exemption based on commerciality the government's practice of buying sporadically in very large quantites can severly impact on a part's commerciality. FAR 15.804-3 says that at a minimum 35% of sales must be commercial if the part is to receive an exemption, but large purchases skew reality For example, say a firm has sold a product into the commercial market at a rate of 1,000 a year. Suddenly it receives a government contract for 4,000. Although it is still basically a commercial part this purchase will compromise commerciality for some time to come.

c. Improper Requests for Cost and Pricing Data

In addition some governmental agencies request cost and pricing data based on local regulations which are contrary to the basic requirements of the FAR and Department of Defense directives. The FAR states in Part 15.804-3 that contracting officers shall not require cost or pricing data when adequate price competition exists which is defined as two responsive, responsible bidders. Be that as it may, some agencies have issued local regulations which require the submission of cost and pricing data regardless of the size of the solicitation and whether competition can be expected.

d. Promotional Prices

As is common with many firms Midland has several published price levels for sales to the general public. These range from list to special promotions which are set for a specific purpose for a short period of time. On occasion these sales appear on a request for exemption which can lead a government agency or prime contractor to insist they be given the same promotional prices on long term contracts. This is unacceptable. If the customer does not withdraw his demand we would forgo the business.

VI. CONTRACT MANAGEMENT

Poor government contract management practices also reduce the attractiveness of government business. Some examples:

a. Length of time to award contracts

The government frequently takes an exorbitant length of time to award a contract. We are still awaiting a decision on a solicitation which closed on February 4, 1988. I do not know what remains to be evaluated after 14 months, but it is still "under evaluation". Although small purchases are processed relatively promptly, this phenomena is not uncommon on larger repair parts procurements.

b. Ridiculously Small Order Quantities

On many occasions Midland has received full solicitations for minuscule quantities of very inexpensive parts. The five cent O-rings are a case in point. One has little interest in a solicitation for four packed A over A to MIL-STD-2703. Were one to calculate the true acquisition cost of those O-rings including the costs of the agency and vendor the $500 hammer would blush.

c. Quality Assurance Representatives

While Midland recognizes that one always deals with individual personalities, there are some real princesses among the government inspectors. These individuals have power far beyond their nominal position and abuse of that power is not unknown. All too frequently they attempt to impose their own requirements on a contract far beyond those stated in the contract and its quality assurance provisions. This can result in large amounts of inventory sitting around awaiting shipment while the QAR, his supervisor, contracting officers and our people sort things out. We have witnessed bickering between our government inspectors and those of a prime contractor over trivial points of protocol which have left us with goods on the dock and our customer with his line down.

VII. SOCIAL AND COMPLIANCE PROGRAM REQUIREMENTS

Yet another source of frustration are social and compliance program requirements.

a. Small Business Subcontracting Plans

Midland could not survive without the small business community; no major corporation can . Roughly two thirds of our outside purchases come from small business. Reporting on small business purchases is another thing. Collecting and reporting this data is time consuming, unproductive and an incredible nuisance.

b. Small Disadvantaged Business Subcontracting Goals

Congress has mandated the development of minority owned business as a social goal. However setting goal levels for minority subcontracting is unrealistic. The automotive industry is competitive and capital intensive. All else being equal a manufacture will buy from that vendor which offers the most favorable product considering quality, price, and delivery regardless of ownership. At present the market has few minority vendors. To require a level of small disadvantaged business participation beyond that which exists in the market place is unproductive.

c. Domestic Bearing Requirement

This recently announced rule is another example of the sort of interference which makes government contracting less than attractive to commercial enterprises. The government's concern over the health of the domestic bearing industry is understandable. However as has been pointed out in a highly competitive industry purchasing decisions are driven by price, all else being equal. If domestic sources cannot pass muster, they must either improve or perish. This is the essence of competition which is the foundation of our capitalist economic system.

Midland, as an aggressive player in the automotive market, constantly seeks the highest quality vendors at the lowest cost. The location of the source is irrelevant. If bearings can be purchased less expensively offshore these savings can be passed along to our customers. To mandate the use of domestic bearings requires the establishment of a special part number with a special bill of material and special manufacturing management. In short, another manufacturing nightmare. Not that this cannot be done but it adds cost, demands special management attention, and is beyond the scope of routine business.

d. Certifications

Without belaboring the point the seemingly endless number of certifications required in government contracting further serve to deter the commercial enterprise from participating in the market.

VIII. CONCLUSIONS

What both industry and the government need are intelligent, consistent specifications consistently applied within contracts which are awarded and administered with good sense and judgement and a minimum of micromanagement, of both the private contractor and contracting officer.

a. Specifications

Industry's participation in the development of performance specifications is imperative if they are to be effective. The TACOM experience is instructive. They should be adaptable so that similar items can be easily bought under the specifications. They should also be consistent within a particular category of items.

Design specifications are not a panacea for all the government's procurement woes. However, carefully drafted and appropriately applied they can do much to remove some of the barriers to market entry which should increase competition, improve quality, and expand the available industrial base.

b. Bureaucracy

In better or for worse we have institutionalized a bureaucracy that rewards conservatism, inaction and inefficency. There are sizable vested interests that have no desire to see change as change represents personal risk. As one individual said, "I'm here for my gold watch and I'll do nothing to risk it". With that mindset entrenched in the lower echelons little will change. The bureaucracy well knows that Legislators, Secretaries and Flag Officers come and go, but it is forever. Furthermore that mindset fosters imcompetence as all too often the brightest bureaucratic recruits, after recognizing the situation, leave and the dullest remain behind.

So what is to be done? The system needs massive renovation. Initative, imagination and reasoned risk-taking need to recognized as desirable professional characteristics and promptly and publically rewarded. Contracting officers must exert their authority, challenging and overruling "experts" where appropriate. Experts have a corporate interest in making things as complicated as possible so they become essential. Incompetence and indolence should be punished - severely. Unless the presently held institutional values change, nothing will happen no matter what Congress does.

c. Government Credability

Last, but by no means least, if the government wishes to avail itself of commercial products, it must convince private industry that it wants to do business with the government. A recent Center for Strategic and International Studies report indicate the number of domestic firms doing business with the Department of Defense declined from 118,000 in 1982 to less than 40,000 in 1987. If these figures are any near correct, the governemnt has a problem.

Even if the government were to commit to reducing micromanagement, professionalizing the bureaucracy, and improving specfications, would industry believe it? Probably not; we have heard Chicken Little too often. Administrations and flag officers come and go, each with their buzz words and new agendas which on closer examination all too frequently appear remarkably similar to the old agendas. Buzz words and reorganizations are wonderful ways of creating the illusion of progress while the essence remains constant. Industry wants deeds, not words.

Beyond that, foreign governments appear to treat their industrial bases as national assets. Here the attitude is adversarial. That may not be the intent, but that is the perception and perception is reality. Life has enough complications without deliberately courting more. Given the complexites and risks associated with government contracting, who needs it?

HEARINGS BEFORE THE SENATE GOVERNMENTAL AFFAIRS SUBCOMMITTEE ON OVERSIGHT OF GOVERNMENT MANAGEMENT

TESTIMONY ON THE ACQUISITION OF COMMERCIAL PRODUCTS

B. DAN PINICK
SENIOR VICE PRESIDENT
THE BOEING COMPANY
AND
PRESIDENT, BOEING AEROSPACE & ELECTRONICS

REPRESENTING

ELECTRONIC INDUSTRIES ASSOCIATION

MAY 16, 1989

Good morning. My name is Dan Pinick, I am a Senior Vice President of The Boeing Company and President of Boeing Aerospace and Electronics. Today I am here representing the Electronic Industries Association. I am pleased to be here this morning to discuss some of the impediments to the acquisition of commercial products by the United States Government. I believe industry, Congress and the DoD agree that appropriate use of commercial and other nondevelopmental products by the Government to fulfill Government requirements could significantly reduce the cost of those requirements, reduce acquisition time and provide operationally-proven quality items for Government needs.

The benefits of using commercial products have been studied as early as 1972, and as late as 1986, when the President's Blue Ribbon Commission on Defense Management (the Packard Commission) recommended the expanded use of commercial products and "commercial-style" competition in the defense procurement process. Thereafter, the 99th Congress enacted a law requiring a "preference for nondevelopmental items" (commercial products) and the FY89 Office of Federal Procurement Policy Reauthorization Act included a requirement to establish an advocate for the acquisition of commercial products. Therefore I will not dwell on the benefits of using commercial products on the assumption that their utility has been recognized. Instead, I will focus on several problems that need to be solved before these benefits can be fully realized.

Before going any further, I would like to explain the dual marketplaces served by The Boeing Company. First, The Boeing Company is the largest producer of commercial aircraft in the free world. Currently, about seventy percent (70%) of our total corporate sales is to commercial customers. At the same time, The Boeing Company is a major defense contractor. We are traditionally one of the top ten defense prime contractors.

For the most part, our Government effort is separate from our commercial activity. Our Government divisions do business with the Government and have the resources and the expertise in place to comply with the military-peculiar requirements in Government contracting. Our Commercial Airplanes division has supported the sale of military commercial products in the past, such as 707s used for AWACs and E-6; and 747s used for E-4, Air Force One, and NASA's Space Shuttle program. We would like to continue selling commercial aircraft to the Government because we believe our commercial products offer many benefits in terms of quality, performance, availability and price.

We have experienced significant problems in our Commercial Airplanes division when supporting the sale of commercial aircraft to the Government. One of the most significant problems is the flow down of Government contract terms and conditions to our suppliers. Many suppliers to the Boeing Commercial Airplanes division are commercial companies or divisions who do no business with the Government. The relationships we have with these suppliers have existed for many years and we look upon our suppliers as partners and an arm of our production capability. These long-term partnerships have resulted in our mutual success in producing innovative, high-quality commercial aircraft at prices established by the competitive, commercial marketplace. Many of these suppliers are accustomed to operating only in the commercial world using commercial business arrangements and are not inclined to reorganize themselves to do business with the United States Government.

Under the current Government acquisition system when we receive a contract for commercial aircraft, there are many Government-peculiar terms, conditions and specifications that we are required to flow down to subcontractors, vendors and suppliers. In many cases the requirement to flow down these terms and conditions finds its origin in United States statutes. In some cases, such as cost or pricing data, there are exemptions that may be available for commercial products. However, qualifying for these exemptions is often difficult, and as a practical matter may not be available. Moreover, the myriad of remaining clauses and Government specifications are generally unacceptable to our commercial suppliers because they are organized to produce and sell their products using commercial business arrangements.

These flow down requirements are a particular problem because of the way in which commercial programs are developed. In a commercial environment, the selection of sources and the acquisition process for raw materials, parts, subassemblies and components is set in motion and often completed well in advance of the orders being placed by the commercial customers. The Government order containing flow down requirements cannot therefore, in many instances, be complied with after-the-fact by our suppliers and vendors. As I indicated, in most of these cases, there is no practical waiver or deviation authority for commercial products. Even where waiver and deviation authority is available to the DoD, there is a general reluctance to pursue those waivers and deviations, especially where the procuring activity is required to elevate the matter to the Head of the Agency. Taken to their extreme, flow down requirements can create an absolute barrier to purchase of commercial aircraft and commercial spare parts.

Furthermore, the problem does not end with the delivery of the aircraft. The problem continues for many years because of the Government's spare parts requirements to support the aircraft.

Boeing's recent experience in attempting to sell a commercial aircraft to the Government was our bid for the Navy's Long Range Air ASW Capability Aircraft (LRAACA). Boeing's proposal for the aircraft was based on the use of a modified version of the 757 commercial jet airliner. At the time of the proposal to the Navy, the commercial 757 was a program that had been in existence for about ten years. This means that Boeing's network of suppliers and vendors supporting the 757 was firmly established with contractual arrangements in place.

For this reason, Boeing proposed that certain Government contract clauses and military specifications typically applied to new Government-designed aircraft be waived. Boeing anticipated that this approach, which met or exceeded the Navy's operational requirements, would allow the Navy to benefit from the advantages offered by the 757's established commercial production and supplier environment.

Nineteen Federal Acquisition Regulation (FAR) clauses (attached) were identified by Boeing as requiring flow down and in order to comply with all the Government flow down requirements would have meant reopening and attempting to renegotiate approximately 3,900 vendor contracts, most of which had been in place since the beginning of the 757 program.

RECOMMENDATION:

We believe there is a large base of high-quality commercial suppliers to which the U.S. Government may not have access because of the terms and conditions associated with Government contracts. Ideally, Congressional preference for the acquisition of commercial products and nondevelopmental items could, to a large measure, be achieved through meaningful regulatory reform. However, this simply has not occurred.

Therefore, we perceive a need for new legislation permitting the acquisition of commercial products with the standard commercial terms and conditions used by the manufacturer of the product.

Recognizing this is a major departure from policies that currently exist and that there may be concerns regarding such a dramatic change, perhaps a trial program could be established, with results to be evaluated following a reasonable period of time. To accommodate this program, I recommend the creation of a Commercial Procurement Authority whose office would be empowered to specifically and exclusively utilize the enabling commercial products legislation. In this way, the interest of the Government would be protected in that the program would be controlled and the results known without having permanently changed the entire acquisition process.

One possible approach to the problem is to statutorily provide for waiver of flow down requirements where the product has met the test of "commerciality" on the same basis as for obtaining an exemption from the requirement to submit cost or pricing data. It is already recognized (under law and regulation) that if a product has a price that is "based on established catalog or market prices" and is sold in "substantial quantities" to the "general public", the Government need not require the submission or certification of cost or pricing data. In turn, it appears logical that the manufacturer of this same commercial product should be equally relieved of other obligations that are inconsistent with commercial terms.

Critical to this approach, however, is the need to further clarify and broaden the definition as to what constitutes the "commerciality" of a particular product. This can be done by redefining some of the terms having to do with commerciality in the Federal Acquisition Regulation.

OTHER RECOMMENDATIONS:

Short of such a broad legislative initiative, there is no way to completely eliminate these problems. Nevertheless, let me suggest changes that can make a difference even under existing law.

First, appropriate language should be added to the Federal Acquisition Regulations which recognizes that in those situations where the Government acquisition includes materials, parts, subassemblies and components that have been routinely produced and ordered by a manufacturer as part of its ongoing commercial activities, the suppliers and vendors of the prime contractor shall not be considered "subcontractors" for purposes of flow down of Government terms and conditions. This would help eliminate the "after-the-fact" imposition of Government flow down requirements.

Second, when commercial sources are known to exist that meet Government requirements, the Government's acquisition plan should encourage the Services to use all available waiver authority requested by the prime contractor and its suppliers and vendors of commercial products.

Third, the DoD should establish a high-level Commercial Products Advocate to work with the OFPP Advocate required by the FY89 OFPP Reauthorization Act to:

(1) Review all proposed procurement regulations to determine those which encourage or discourage the acquisition of commercial products.

(2) Provide recommendations to the Secretary of Defense and the Administrator OFPP, as to what statutes and procurement regulations should be rescinded or modified to encourage the acquisition of commercial products.

(3) Provide recommendations as to methods for simplifying procurement regulations governing the acquisition of commercial products.

In conclusion, I'd like to again point out that without statutory enabling language which, while preserving other public policies, creates a vehicle for awarding Government contracts for selected commercial products using those terms, conditions and specifications that are used by the manufacturer of the product in the commercial marketplace, the Government will not adequately benefit from the use of high quality commercial products at competitive prices.

Thank you very much for providing me the opportunity to present our views on this important issue. I would be pleased to answer any questions you may have.

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Attachment to
B. Dan Pinick
Testimony on the Acquisition
of Commercial Products

TITLE	CLAUSE
RESTRICTIONS ON SUBCONTRACTOR SALES TO THE GOVERNMENT	FAR 52.203-6
ANTI-KICKBACK PROCEDURES	FAR 52.203-7
PRIORITIES, ALLOCATIONS AND ALLOTMENTS	FAR 52.212-8
EXAMINATION OF RECORDS BY COMPTROLLER GENERAL	FAR 52.215-1
SUBCONTRACTOR COST OR PRICING DATA	FAR 52.215-24
SUBCONTRACTOR COST OR PRICING DATA-MODS	FAR 52.215-25
UTILIZATION OF SMALL BUSINESS CONCERNS AND SMALL DISADVANTAGED BUSINESS CONCERNS	FAR 52.219-8
SMALL BUSINESS AND SMALL DISADVANTAGED BUSINESS SUBCONTRACTING PLAN	FAR 52.219-9
UTILIZATION OF LABOR SURPLUS AREA CONCERNS	FAR 52.220-3
LABOR SURPLUS AREA SUBCONTRACTING PROGRAM	FAR 52.220-4
CERTIFICATION OF NONSEGREGATED FACILITIES	FAR 52.222-21
EQUAL OPPORTUNITY	FAR 52.222-26
AFFIRMATIVE ACTION FOR SPECIAL DISABLED AND VIETNAM ERA VETERANS	FAR 52.222-35
AFFIRMATIVE ACTION FOR HANDICAPPED WORKERS	FAR 52.222-36
CLEAN AIR & WATER	FAR 52.223-1, 2
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ADMINISTRATION OF COST ACCOUNTING STANDARDS	FAR 52.230-4
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HEARINGS BEFORE THE SENATE GOVERNMENTAL AFFAIRS

SUBCOMMITTEE ON OVERSIGHT OF GOVERNMENT MANAGEMENT

TESTIMONY ON THE ACQUISITION OF COMMERCIAL PRODUCTS

NAOMI M. WILLIAMSON
MANAGER, CONTRACT MANAGEMENT
HONEYWELL INC.
SPERRY COMMERCIAL FLIGHT SYSTEMS GROUP
BUSINESS & COMMUTER AVIATION SYSTEMS DIVISION

REPRESENTING

ELECTRONIC INDUSTRIES ASSOCIATION

MAY 16, 1989

Good morning. I am Naomi Williamson, Manager of Contracts for the Business and Commuter Aviation Systems Division (BCASD) of Honeywell and I am here representing the Electronic Industries Association. Honeywell applauds efforts to encourage Government procurement of commercial and nondevelopmental items to save money and take advantage of technological advances that are available in the marketplace. My purpose in attending this hearing is to share some of Honeywell's experiences as a commercial contractor with whom the Government or Government primes have tried to contract. I hope our experiences will help illustrate some of the problems that must be solved in order for the commercial procurement initiatives, like those recommended by the Packard Commission, to succeed.

Because Honeywell is a well known defense contractor, you might think that knowledge of Government procurement regulations transfers from the defense divisions to the commercial divisions. Actually, it does not as there typically is no need for it. Honeywell's defense divisions have expertise in the regulations and comply with the Government terms of doing business--but the commercial and defense divisions operate quite independently from each other. Therefore, the experiences I plan to share with with you today should be similar to those any commercial contractor would face with Government procurements. Let me start with a brief description of our products and marketplace.

BCASD designs, develops, integrates and manufacturers avionics systems for executive aircraft and commuter aircraft--aircraft small than Boeing or McDonnell Douglas air transport aircraft, but more expensive than small general aviation aircraft, such as two to four seat Cessna or Piper aircraft. Examples of the aircraft manufacturers with whom we contract are: Gulfstream, Dassault, Aerospatiale, Canadair, Fokker, deHavilland, British Aerospace, Beech, and Cessna. We also have a dealer network and a product support network for the businesses and airlines that use our equipment.

BCASD was formed specifically to answer the demand this market has for lower cost avionics combined with quick response time for implementation of new features demanded by corporate pilots.

Generally, our products include sensors, controls and cockpit displays. Examples are: Automatic Flight Control Systems; Electronic Flight Instrument Systems (EFIS); Flight Management Systems; Radios; Air Data Computers; Inertial Reference Systems; Color Weather Radar, etc.

BCASD employs approximately 1400 people. In 1988, approximately .3% of the Division's revenue resulted from sales to the U.S. Government (e.g. inertial systems or radars) or for Government end use (e.g. Beech aircraft sold to the Air Force). We anticipate that U.S. Government/military customer revenue for 1989 will be approximately .7%. Such sales are accomplished generally by use of Standard Form 1412. Subject to export control, we sell products directly to foreign military customers using standard commercial terms.

I am here to talk about a recent experience BCASD had with attempting to sell commercial avionics to a Government prime for a Navy program.

THE LOCKHEED/BCASD EXPERIENCE ON THE LRAACA PROCUREMENT

After investing over two years of time and effort in pursuit of a subcontract with Lockheed for the avionics for the Navy's LRAACA (Long Range Air ASW (AntiSubmarine Warfare) Capability Aircraft) Program, on the eve of contract negotiations and award our Division made the difficult decision to withdraw our bid.

HISTORY OF THE BID

During the fall of 1986, Lockheed contacted our Division because the Navy had encouraged consideration of a commercially available Electronic Flight Instrument System for the LRAACA aircraft. The other companies from whom the Navy sought bids for the prime contract were the commercial aircraft divisions of Boeing and McDonnell Douglas. Lockheed was the only company that bid the program from a division that primarily does defense contracts.

In early 1987, Lockheed requested a presentation on the systems we could offer for use in their bid to the Navy. We gave a technology presentation showing our state-of-the-art systems on the Gulfstream IV aircraft. Those systems included six 8" x 8" CRT displays (glass cockpit) and a comprehensive integrated avionics system.

We had early discussions with Lockheed on the contracting issues. Lockheed assured us that they were under instruction from the Navy to consider commercial products and felt that to be competitive with other bidders, they would have to offer commercial avionics. Because of the Navy's stated preference for a commercial EFIS they were confident the Navy would help them resolve any commercial contracting issues that might arise on the program. We each thought the other understood what was meant by "commercial" contract terms. It was much later that we came to understand just how dissimilar our understandings were.

In October of 1987, BCASD submitted the first proposal for a comprehensive integrated system based on the Gulfstream IV system.

In May 1988, the formal Request for Proposal was received for five of the systems: Electronic Display System, Flight Management System, Microwave Landing System, Color Weather Radar System, and Passive Weather Avoidance. The RFP contained a subcontract section with an entire complement of FAR, DFAR and NAVAIR clauses incorporated by reference--and included throughout the text of the contract.

We objected and Lockheed explained that under the rules for a commercial exemption on the basis of competition, they had to give exactly the same package to all bidders. They acknowledged that they had said they would contract with us on commercial terms, but explained that the only way they could show that they ran an equal competition would be to show that everyone responded to the same package. They asked that we review the contract and take exception to anything that would not apply. It was during review of this contract that we became very concerned. Top management meetings took place between Lockheed and our Division to make sure Lockheed clearly understood that our position against accepting Government flow-down terms was absolute.

We asked whether the Navy could be approached for an early determination regarding issues of commercial contracting terms. Since Lockheed was itself in a tight competition, they were hesitant to do anything that might be construed as controversial or that might have an adverse effect on the Navy's view of their proposal. Lockheed promised to pursue resolution of the commercial contracting issues on our behalf the moment the program was awarded to them. Based on these assurances, we continued to work on our proposal.

In June of 1988, we submitted our Proposal. We stated clearly that we were responding to the military subcontract as an accommodation to Lockheed for competitive evaluation purposes and that we would be unable to accept any contract that contained requirements for cost reports, cost audit rights, quality audit and many other Government terms.

We than sent our engineers to work full time at Lockheed's facilities to assist Lockheed in preparing its proposal to the Navy.

In August we submitted our Best and Final Offer. Our final proposal contained 22 major part numbers, 7 of which might require modification (from 0% minimum to 40% maximum) for the mission and aerodynamic requirements of the aircraft.

Lockheed submitted their proposal to the Navy with a picture of our Cockpit Displays on the cover of each volume of the proposal.

Lockheed was selected by the Navy.

December 21, 1988, Lockheed submitted to the Navy a request for waiver of Government contracting terms flow-down for their subcontract with the Division.

CONTRACTUAL DIFFERENCES BETWEEN WHAT LOCKHEED GAVE US AND WHAT WE RECEIVE NORMALLY

The task of reviewing the 88 page Lockheed subcontract was monumental for a Division whose normal contract is less than 40 pages long and does not incorporate by reference a book of fine print regulations, additional special defense regulations, and additional special Navy clauses. We had no one on staff to review the contract who had current knowledge of the entire Federal procurement regulation structure. But we were not overly concerned because we believed that if we were awarded the job, Lockheed understood that a commercial contract (meaning to us standard Uniform Commercial Code terms) would be used and the Navy would support Lockheed because they had requested commercial avionics.

We made 83 exceptions or changes to the subcontract because terms were inapplicable, inconsistent with the way we do business, or inconsistent with commercial contracting terms. That means we took exception to mandatory terms right along with the rest. Examples of the Clauses we identified as inapplicable, objected to or changed follow:

Required Sources for: Miniature and Instrument Ball Bearings,
    Precision Components,
    High-Purity Silicone, and
    Jewel Bearings
    High Carbon Ferrochrome
Tooling and Material
Special Tooling and Special Test Equipment
Parts Control Program
Security Requirements
Facilities Provided by Contractor
Government Property
Modifications
Rights in Technical Data
Termination
Warranty
Incremental Funding and Schedule Adjustments
Examination of Records by Comptroller General
Audit-Negotiation
Price Reduction for Defective Cost or Pricing Data
Subcontractor Cost or Pricing Data

Cost Accounting Standards
Subcontracts Under Fixed Price Contracts
Restrictions on Subcontractor Sales to the Government
Small Business and Small Disadvantaged Business Subcontracting Plan
Labor Surplus Area Subcontracting Program
Patent Rights (annual report)

After we had put together our response and were about to submit our BAFO, it finally occurred to us that we might be in for more difficulty than we thought over the commercial contracting issues. We turned for help to our Corporate Contract Management staff and the Office of General Counsel: a resource I doubt most commercial contractors have. Of course, when they read through the list of exceptions we had taken, they raised a red flag. They advised that Lockheed could not do what we had asked them to do--not if the procurement was to be accomplished pursuant to the Federal Regulations. There is no such thing as a "commercial contract" exemption under the existing regulations. We also hired outside counsel to advise us and got the same answer.

Still trying to achieve a mutually acceptable method of contracting, we requested that a review team be put together of Government contracting experts and our commercial contracting representatives.

THE DIFFERENCE BETWEEN COMMERCIAL AND MILITARY BUSINESS

A couple of preliminary comments here might further help to understand the critical differences in how we approach our market and contracts and how a Government contractor analyzes contract terms. We look at the market, determine what might sell, develop product concepts, write the specification (we are the experts), build prototypes and present the product to the marketplace. If customers want the product, we charge them non-recurring costs adapt the product to their specific application and requirements.

Prices are only partly affected by cost. They are set by what the market is willing to pay. For large programs, prices are usually based on targets set by customers and negotiations regarding what we can provide for what the customer wants to spend. Many factors affect the pricing decisions including: knowledge of what the competition has to offer, customer's budget, customer's strategic importance, probably success of the customer's aircraft, unseating a competing incumbent supplier, and the probability of recovering our investment and making a sufficient profit to allow further investment in other products and programs.

Contract terms in a commercial environment are business decisions (can we do it and are we willing to do it?). Failure to comply results in liquidated damages or a breach of contract lawsuit. The focus remains on efficiency (accomplishing the most with the fewest people) in order to keep the cost of doing business down and stay competitive in the marketplace. In contrast, contract terms in the Government environment are legal issues (can the Government require us to do this?) with a strong focus on compliance issues because failure to comply can result in criminal prosecution of both the contractor and the Procurement Contracting Officer.

WHY WE COULDN'T DO IT

First, Government contracting is a way of life. Virtually every detail of how to operate a business has a regulation that will apply. The people who work in our division--from engineers, marketers, and accountants to assemblers--are not familiar with Government contracting methods of doing business. This substantially increases the risk of inadvertent noncompliance, for example, the idea that uncompensated overtime is somehow unacceptable would surprise nearly every exempt employee in our division.

The LRAACA review team analyzed the issues and risks from a long term standpoint, not just a program award standpoint. As hard as we tried, we could identify no way to limit risks with this program other than to set up a separate business entity with its own manufacturing facilities, engineers, accountants, contract managers, etc. The specific issues follow:

I. AUDITABLE CERTIFIED COST OR PRICING DATA REQUIREMENTS

A. The Competition Exemption

We had been told that the Navy Prime contract was to be awarded pursuant to the competition exemption from the requirement for cost or pricing data. The competitive exemption on the initial purchase was the only commercial contracting issue solved by the regulations. PCO's, however, do not seem to be able to administer this exemption, i.e., there is no certified piece of paper to put in the file for each part number. For example, Lockheed was awarded the

Navy program and was not required to provide cost or pricing data. After we had withdrawn our bid, Lockheed asked if we would be willing to supply three of the systems we had bid that would not have to be modified. Lockheed needed to order a few systems to support the FSED part of the program. In spite of contract award pursuant to the competition exemption, the PCO stated that Lockheed would be required to obtain cost or pricing data or a SF1412 from us. It is also clear from the letter that the PCO did not understand that a SF1412 and a waiver are not the same. We would not have needed to ask for waiver of Government contracting requirements if we could have solved our problems with SF1412.

B. Limitations of the SF1412

In our experience with Government sales, PCO's uniformly believe that the only way they can purchase a commercial product is by putting a SF1412 in their file. Unfortunately, the SF1412 cannot often be used for our sales. For example, at this point it is impossible for us to comply with the SF1412's requirements for Lockheed's procurement of the three unmodified systems they still want to buy from us. Even though we do not have to modify these particular products for Lockheed, these are new systems recently introduced to the market. Therefore, these systems do not yet have a substantial sales history.

There will be a limited period of time when the products probably will qualify for sale using a SF1412, but at any point in time there is a risk we would be unable to use that form. Any of the following will prohibit us from selling to the Government if SF1412 is the only method for accomplishing the sale: sales based on catalog price fall below what can be considered "substantial"; sales to the Government exceed 45%; not a wide enough variety of commercial customers buy that specific part number; or, the commercial market stops buying that part and moves on to a different technology. For the supply of avionics which must be engineered at significant cost into aircraft systems, the SF1412 is an inadequate vehicle for assuring that the Government can obtain an uninterrupted supply of product.

1. Why SF1412 is inadequate for the LRAACA program

For the LRAACA program, 1412s would be insufficient at several stages of the Program. At the beginning of the program, any newly developed parts would not qualify. Throughout the program, parts modified to the aircraft application would be required to have unique part numbers for safety reasons and, therefore, would not qualify for exemption. Some of the parts that would not need to be modified are sold to only one other customer (Gulfstream) and, therefore, would not qualify. Aircraft production is scheduled to start in 1995, after or near the end of Gulfstream IV aircraft production; at that point, the majority of sales would have been to the Government. And, two years after substantial general public sales ended, the commercial contractor cannot use past commercial sales to qualify for exemption.

2. Direct purchase of spares by Government

All the above limitations would have made purchase of spares directly by the Government an impossibility for the LRAACA program. To avoid the issue, we stated in our proposal that we would sell spares for the Government to Lockheed at Lockheed's price. Lockheed said this was an issue between us and the Navy.

3. Air Force Example

One example of the application of the the restrictive rules of the SF1412 occurred recently when the Air Force tried to order, for a Foreign Military Sale, four parts that make up a particular weather radar system. Two of the four parts could not qualify for the 1412 exemption (enough customers but insufficient quantities). The PCO solved one problem by buying a smaller, less desirable display that could qualify for the exemption. A fourth part (an $1,807.00 flat plate antenna) required for system operation, has not yet been defined as it does not qualify for SF1412 exemption. We are the only supplier. The irony is that the Foreign Military customer could have purchased the part directly from us without a problem.

4. How much modification can be accepted?

Minor product modifications can be accepted at the discretion of the contracting officer (and the auditor). There is no real guidance for how much modification is too much. Lockheed chose to establish a guideline of 40% for this procurement.

5. Auditing standards are inconsistent

The final problem we face with the SF1412 is with inconsistent auditing standards. Some auditors will allow price justification based on catalog when a distribution of prices around catalog price is demonstrated. Others will deny any sales not exactly at catalog price. Some auditors will allow similar product sales histories to be used to justify the price to the Government. Others require strict sales history on only that detailed part number. The applicable rules are not defined at the time of bid soliciation.

C. NON-RECURRING CHARGES FOR CHANGES

Even if the initial contract awarded would have been accomplished under the competition exemption from the requirement for cost or pricing data, that would not have resolved many other commercial contracting issues. The most important single issue in this category is the requirement for certified auditable cost or pricing data for engineering changes and termination claims. Changes could not have been avoided on the LRAACA program. Avionics must be tailored to the aerodynamics and mission requirements of the aircraft and interfaced with the other systems on the aircraft. During the development phase, these items get refined. If the change is out of the scope of the job the contractor originally bid, then the contractor is due an equitable adjustment. Further, the Government has the right to unilaterally direct changes for any part purchased only by the Government. Auditable certified cost data must be supplied if the dollar threshold is reached.

Our accounting system is not CAS compliant. We do not employ accounting staff to host Government audits of our books. Once the right to audit has been granted, it is very difficult to limit an auditor's demands or contain the added cost of doing business that comes from additional reports and the infrastructure to support an audit.

In our LRAACA bid, we did not ask that our Change quotes be accepted at face value. We proposed the same substitute reasonableness/fact-finding procedure we offer for our major commercial contracts.

C. OPTION EXERCISE

The exemption based on competition does not grant any protection to the commercial contractor that firm option prices will be accepted by the PCO or auditors when the option exercise date arrives. The PCO has the right to require new cost or pricing data. We tried to address this issue by firm pricing the options including an escalation formula. We added a provision assuring Lockheed that if the formula yielded a higher price for any part sold to Lockheed than the catalog price for similar parts, we would lower the price to Lockheed to the catalog price. Our intention was to make sure that marketplace forces affecting even similar parts would continue to protect Lockheed and the Navy.

D. RISK TO OTHER DIVISIONS

Some of the products we were going to be selling to Lockheed include products built by other commercial divisions of Honeywell. If any of the requirements for auditable certified cost data flowed down to us, they would not have stopped with our division. Other commercial divisions would have been forced to comply or refuse to sell to us.

II. DATA RIGHTS

The regulations required Lockheed to obtain design data if any Navy funded non-recurring was paid. Designing the modifications to the avionics to fit the aircraft and its mission would require non-recurring investment. We were willing to invest some of our own money, but not to fund it all. Therefore, because some Navy funds would have been paid, we could lost rights to designs funded by us.

Data and training to be provided to the Navy was also an issue. Some of the requests were for data we consider proprietary and will not provide.

III. PROGRAM MANAGEMENT

In the course of our dealings with Lockheed, it eventually became clear that once the subcontract was awarded and performance began, there would be constant reference to FAR and DFAR provisions. We were going to be faced with explaining our position again and again whenever an issue arose regarding compliance with Government practice.

CONCLUSION

When we bid this program, we thought a "commercial contract" was one based on terms like the Uniform Commercial Code and other mutually acceptable conditions. Lockheed thought they could find enough exemptions in the FARs to be able to award the subcontract to us. We tried to find a way to accomplish acceptable solutions under the existing set of Government contracting regulations. Ultimately, there were just too many issues, too many risks, too much probability that this subcontract could force us into adopting Government contracting business practices. This eventually would drive us out of our primary served market. Even trying to set up a separate business entity - which is what all the experts recommended - did not adequately address interdivisional pricing issues and would have destroyed the economies of scale that incremental business brings.

We have hope that some of the problems we have experienced are being recognized and addressed. For example, the Air Force in the Tanker, Transport, Training System procurement, has taken some very promising steps toward resolving these issues before the actual Air Force RFP is issued. This is the result of much effort by both industry and the Air Force, but the issues are addressed on an exception basis. While we appreciate the Air Force's effort and willingness to work the issues, using a case-by-case approach is not the solution. Nor can these issues be addressed piecemeal by trying to amend each of the laws and regulations that prohibit or impede government procurement of commercial products.

RECOMMENDATION

For the benefit of both government and industry, we need laws that allow the Government to procure commercial products using commercial terms.

Thank you for allowing us to share this experience and our views with the committee. I would be pleased to answer any questions you may have.

TESTIMONY OF

JOHN M. FLUKE, JR.
CHAIRMAN OF THE BOARD
JOHN FLUKE MFG. CO.
CHAIRMAN OF COMPACT

Mr. Chairman, Members of the Subcommittee, my name is John Fluke. I am Chairman of the Board of the John Fluke Manufacturing Company. I also have the privilege of serving as Chairman of the Commercial Product Acquisition Team.

The Fluke Company manufacturers and distributes a wide range of commercial electronic test, measurement and diagnostic equipment. Last year we had sales of about $225 million. Of that, about 15 percent was in direct sales to the federal government and about 12 percent was in sales to federal government prime contractors. We view the government as an important and significant customer, but at the same time, we build and design our products to meet the needs of all of our customers in the commercial marketplace.

We very much appreciate the opportunity to testify before you today. It has been just over three years since COMPACT last testified before Congress on the issue of commercial product acquisition by the federal government. As you may recall, it was in March of 1986 that COMPACT appeared before then-Senator Quayle and you, Mr. Chairman, on the Subcommittee on Defense Acquisition Policy of the Armed Services Committee. We supported at that time the Levin Legislation that, when enacted later that year, established for the first time a statutory preference for the acquisition of commercial products.

As indicated in our written statement, we consider the enactment of the Levin Legislation to have been the positive force in helping to change the procurement environment towards the consideration of the benefits of commercial products. We would like to be able to report to you today that all necessary changes in both regulations and procedures have either occurred or are in the pipe line. We would like to be able to report that all the impediments to a comprehensive commercial product acquisition policy have been identified and are being eliminated.

Unfortunately, no such report can be made. It is absolutely clear that the environment for considering such changes is immeasurably better today than what it was three years ago. However, despite indications that top executive branch procurement policymakers support both the Levin legislation and the basic concepts of buying more commercial products in a more commercial-like manner, too little real action has occurred that affects the day-to-day buying practices of field level government procurement personnel. We view these hearings and your special interest in these issues as supplying the critically needed encouragement to move from the policy stage to the action stage.

I would like to focus this morning on a few of the issues that we believe must be addressed if real improvement is to occur in implementing a comprehensive commercial product acquisition policy.

First, it remains critical that the top level procurement policymakers at the Department of Defense, the Office of Federal Procurement Policy, and other civilian agencies move the issue of commercial product acquisition up on their agendas of action items. Three years ago, commercial product acquisition wasn't even on those agendas; now it is. Partly because commercial product acquisition issues will never attract the type of attention given to big dollar procurement scandals nor is it likely that a single commercial product buy will ever match the billions spent on a single weapon system, policymakers end up liking the issue but have not yet focused on it or devoted significant resources to it.

We note that the Department of Defense seems to vacillate between trying to support the policy and denying that any problems exist. For example, while we appreciate the fact that there is now a position within the Office of the Secretary at DOD that is supposed to advocate commercial product issues, to little action has taken place, in part because too few staff resources have actually been devoted to it and too little coordination of effort by the Services and buying commands have occurred. Until the top policymakers learn the issues and begin to demand solutions to the problems, real improvement will continue to occur in a disjointed and haphazard manner.

Second, there has been a lot of talk about adopting commercial-style practices. We strongly endorse this basic policy and we believe that it will save both the government and commercial vendors significant amounts of money while actually increasing participation in the government marketplace. We have yet to see, however, after three years, a single government document that attempts to identify what those commercial-style practices are and how they can be adopted on a large scale basis by the government. Without such a game plan, we will continue to be subject to limited efforts at improvement and bits and pieces of change.

Hand-in-hand with identifying commercial-style procedures is the need for training field level government procurement personnel in the most efficient manner in which to buy, evaluate and utilize commercial products. The sales forces of almost every commercial vendor regularly face government contracting officers and other procurement personnel that have been trained in and rely on a system designed to buy government-designed products from cost base contractors. Without adequate training in buying commercial products using commercial-style procedures, many of the problems and cost-inefficiencies faced by both the government and commercial vendors will simply continue.

Finally, I would like to address briefly two specific areas of concern that need a considerable amount of attention: rogue contract clauses and the regular demand for cost or pricing data.

The first issue, rogue contract clauses, refers to the fact that a commercial vendor doing business with the government today must be a legal contortionist in order read and understand government contracts. It never ceases to amaze me that what the commercial marketplace can do with a few pages, the government uses up volumes.

For example, COMPACT recently analyzed 7 recent contracts for standard commercial products. According to our analysis, there were 170 different standard Federal Acquisition Regulation clauses that appeared at least once in one of those contracts. There were 53 different standard DOD clauses that appeared at least once in one of those contracts. In addition, there were 34 different standard buying command clauses that appeared at least once in one of those contracts. That is a total of 257 standard clauses.

In addition, almost all of the contracts for standard commercial products referred to military specifications for packaging or manufacturing process controls. Those specifications themselves incorporate other specifications that must be followed in order to ensure complete contract compliance.

COMPACT suggests that the solution to this particular problem is the adoption of a standard form government contract for commercial products. Such a document would incorporate only those clauses required by statute to be incorporated into a contract and would rely on commercial practices to the maximum practicable extent. We note that in our own initial effort at writing such a contract, we have been able to identify only 15 or 20 clauses actually required by statute. So the problem is not with the ways the laws are written, but the way the procurement system and regulations fail to recognize the difference between commercial contracting and cost-base contracting.

The second issue that I want to talk about for a moment is cost or pricing data. The other members of COMPACT will go into more detail on this issue, but I want to highlight one of the problems. That problem is regular request for cost or pricing data on clearly competitive acquisitions. It seems that the original purpose for requesting cost or pricing data has been lost in the attempts by contracting officers to document every acquisition with as much information and data as possible.

The Fluke Company regularly receives request for cost or pricing data and must in turn submit requests for exemption or spend time to eliminate the request through contract negotiation. Our view is that contracting officers are not making such requests because they believe the Fluke Company is charging unreasonable prices, but because those contracting officers are strictly adhering to narrow interpretations of the regulations and simply refuse to exercise reasonable discretion. The result is increased costs for the Company and no added benefit for the government.

Let me again thank you for providing us this opportunity to testify. We look forward to answering any questions you might have and look forward to working with you as efforts are made to induce positive action out of the executive branch agencies.

COMPACT
Commercial Product Acquisition Team
1735 New York Avenue, N.W.
Suite 500
Washington, D.C. 20006
(202) 628-1700

TESTIMONY OF THE

COMMERCIAL PRODUCT ACQUISITION TEAM

(COMPACT)

BEFORE THE

SUBCOMMITTEE ON OVERSIGHT OF GOVERNMENT MANAGEMENT

COMMITTEE ON GOVERNMENTAL AFFAIRS

UNITED STATES SENATE

PRESENTED BY

JOHN M. FLUKE, JR.
CHAIRMAN OF THE BOARD
JOHN FLUKE MFG. CO.
CHAIRMAN OF COMPACT

AL HERMAN
GENERAL MANAGER
FEDERAL SYSTEMS DIVISION
TEKTRONIX, INC.

JOHN MCGOWAN
FEDERAL SYSTEMS MANAGER
HEWLETT PACKARD COMPANY

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I. EXECUTIVE SUMMARY

Mr. Chairman, as representatives of the Commercial Product Acquisition Team (COMPACT), we very much appreciate the opportunity to appear before you today on the subject of commercial product acquisition in the federal government. We believe that it is fair to say that without your leadership in this area, the positive changes that have occurred in the past three years would not have happened. And without your continuing interest, essential changes might not occur.

We are particularly pleased that you have continued your oversight of this very important area of federal procurement policy at this time. Although we are pleased to report that the "environment" for commercial product acquisition has improved since the last time we appeared before you, we are now at a critical stage with an opportunity to see real improvement in the acquisition environment. However, those changes are in need of some additional encouragement by policymakers such as yourself interested in seeing the acquisition environment continually improved.

This morning we would like to discuss the following issues:

- Past Commercial Product Acquisition Policy Efforts;
- Current Commercial Product Acquisition Policy Efforts;
- The Need for Training;
- Existing Regulatory Impediments; and
- Recommendations for Changes.

As you will note, we identify several specific existing regulatory impediments that must be eliminated in order for the federal government to take full advantage of a comprehensive commercial product acquisition policy. Those impediments include:

- Lack of adequate training for government contract personnel in commercial product acquisition techniques;
- Requests for cost or pricing data for commercial products on federal supply schedules; for commercial products being purchased through competitive acquisitions; for commercial products previously acquired in large numbers by the government; for new commercial products; and for spare and replace parts for commercial products;

- Failure to evaluate the costs of ownership and quality costs associated with commercial products;

- Unreasonable use of flow-down clauses in subcontracts;

- Failure to use a standard form government contract for commercial product acquisitions;

- Unnecessary inspection and quality assurance requirements for commercial products; and

- Unnecessary use of the Defense Priorities and Allocations System ratings.

We recommend that Congress take immediate action to require the Department of Defense and other federal agencies to:

- Develop and initiate training programs in commercial product acquisition techniques that cover: market research techniques; commercial product pricing policies; the proper, limited use of cost or pricing data; the proper means of granting exemptions to the submission of cost or pricing data; and the use of commercial-style practices;

- Amend the Federal Acquisition Regulation Subpart 15.8 in order to facilitate the acquisition of commercial products by limiting the number of requests for cost or pricing data as well as establishing reasonable practices for granting exemptions;

- Develop and require the use of a standard form government contract for commercial products;

- Eliminate the need for government inspection of commercial product manufacturing processes and rely on the use of available commercial product warranties; and

- Amend the Defense Priorities and Allocations System regulations so that ratings are used only when justified.

II. PAST COMMERCIAL PRODUCT ACQUISITION POLICY EFFORTS

As you know, the establishment of a comprehensive commercial product acquisition policy in the federal government has been a very long time in arriving. The history of this effort dates back to the 1974 DOD Defense Science Board Task Group on the acquisition of commercial products in the electronic test and measurement industry. John Fluke, Sr. had the privilege of chairing that particular committee. The recommendations they made in 1976, that the federal government should buy more commercial products in a more commercial-like manner, are as relevant today as they were almost 15 years ago.

More recently, COMPACT was organized in 1985 based on the belief of several commercial product vendors interested in doing business with the government that the accumulation of statutory, regulatory and procedural changes associated with the government marketplace had focused almost exclusively on the actions of government contractors doing cost-based contracting. These changes have essentially painted all companies selling products to the government with the same broad brush of reform and have not recognized the fundamental differences when the government does business with commercial product vendors. These changes, coupled with a 30 year history of buying specially designed, government unique products have produced, in many instances, an intolerable situation for most commercial product vendors.

A. Packard Commission

About the same time COMPACT was being organized, former President Reagan established the "President's Blue Ribbon Commission on Defense Management" which became known as the "Packard Commission," named after the Commission's Chairman, David Packard of the Hewlett-Packard Company. One of the Packard Commission's objectives was to develop recommendations on how best to reform DOD's acquisition process in order to improve the process and put an end to the scandals being reviewed by Congress.

COMPACT viewed the efforts of the Packard Commission as an excellent opportunity to elevate official interest in commercial product procurement as a partial solution to acquisition problems as well as a sensible, and cost-effective way of doing business on a daily basis. As its first task, COMPACT prepared and presented to the Packard Commission a detailed report on commercial product acquisition that included several findings and recommendations for changes in statutes, regulations, and procedures.

The Packard Commission adopted the basic findings of the COMPACT report and in its acquisition report to the President made the following recommendations:

> Rather than relying on excessively rigid military specifications, DOD should make much greater use of components, systems, and services available "off the shelf." It should develop new or custom-made items only when it has been established that those readily available are clearly inadequate to meet military requirements.
>
> Federal law and DOD regulations should provide for substantially increased use of commercial-style competition, relying on inherent market forces instead of governmental intervention. To be truly effective, such competition should emphasize quality and established performance as well as price, particularly for R&D and for professional services.

B. Levin Legislation

Following the recommendations of the Packard Commission, as you well know, Congress enacted legislation sponsored by you that established for the first time, a statutory preference for commercial products and other nondevelopmental items. That piece of legislation is viewed as a turning point by COMPACT's in our efforts to improve the government marketplace for commercial products.

Not only did it establish a clear preference, reversing some 30 years of reliance on detailed military and federal design specifications, it also clearly established commercial product acquisition as a policy initiative that was to be implemented at long last. It is interesting to note that where COMPACT often felt alone when it was first organized, we are pleased to note that commercial product acquisition policy has become a priority not only of several industry associations, but of executive branch policymakers as well. We note with some enthusiasm as an example of this improving environment the fact that when the current OMB Director Richard Darman was questioned by the Governmental Affairs Committee for his confirmation hearing, he identified commercial product acquisition as a primary procurement policy interest.

C. Department of Defense Report

In order to track implementation of the policy established by statute, the Levin Legislation required two status reports. The first report from the Secretary of Defense came out in December of 1987 and was to identify actions taken, including the training of personnel and changes in regulations and procurement procedures. In addition, the Secretary was to identify all statutes and regulations that impede the acquisition of commercial products and other nondevelopmental items with recommendations for additional statutory changes. In order to assist DOD in the identification of existing statutory, regulatory, and procedural impediments, COMPACT prepared, in August 1987, a detailed report that identified 35 specific regulatory and procedural impediments and made 36 recommendations for changes.

Unfortunately, the final DOD report was a wholly inadequate response to the statutory requirements. It provided a misleading picture about what actions have been taken to improve the acquisition process and to comply with the new statutory requirements. In addition, the Report did not serve its intended purpose of identifying those regulations and procedures that impede effective commercial product acquisition. The Report only identified five general impediments including a general statement about unnecessary clauses and complex regulations, the Cost Accounting Standards, rights in technical data, the General

Services Administration's Multiple Award Schedule program, and the Truth in Negotiations Act.

With regard to those five impediments, DOD did not identify which contract clauses were unnecessary or which regulations are too complex. DOD did not identify how the CAS standards are, in fact, a problem for commercial product vendors, probably due to the fact that commercial product vendors generally do not compete for CAS covered contracts. DOD correctly identified technical data rights as a serious impediment, but did not identify how best to deal with the very real problems faced by commercial product vendors and government procurement personnel. And although many companies would agree that the MAS program has serious problems, DOD merely stated that they had met with GSA officials and that they had been assured that "most companies" were bidding and participating in the schedule process so therefore there are no real problems. Finally, while DOD correctly identified the Truth In Negotiations Act as an impediment, they failed to address any of the many specific and issues that affect commercial product companies facing Truth in Negotiations Act requirements on a daily basis.

D. General Accounting Office Report

The second report was written by the General Accounting Office. It was intended to review the activities of the Department of Defense in implementing the requirements of the Levin Legislation. Although COMPACT agrees with the basic conclusion of the GAO report that "DOD needs to do more to ensure its requirements for supplies are defined and fulfilled through NDI [Nondevelopmental Items] to the maximum practicable extent," we are disappointed that GAO apparently did not attempt to verify independently through review and audit techniques the status of impediments identified by commercial vendors.

E. Defense Science Board

We are also pleased that the Defense Science Board has continued its efforts of its 1987 Summer Study Task Force on commercial product acquisition. COMPACT was invited to provide the Task Force with specific regulatory changes need to eliminate existing and very troublesome impediments to doing business with DOD. We provided the Task Force with 12 specific regulatory changes that we continue to believe would greatly improve the contracting process while continuing to protect the best interests of the government. We look forward to reviewing the final report of the Task Force due out shortly.

F. Office of Federal Procurement Policy

We also note that the office of Federal Procurement Policy and DOD have been working on legislation for over a year that would establish a separate system for repetitive buys of commercial products based on a number of evaluation factors beyond lowest initial product price. We are encouraged by this effort, although we are also somewhat discouraged by the amount of time it has taken to produce a document that both DOD and OFPP can accept. We look forward to reviewing and commenting on the final product.

Finally, we are encouraged by the creation by Congress of a commercial product acquisition advocate position at OFPP. Such a position can become the focal point for government activity in this area and provide much needed coordination and direction. We are, of course, disappointed that the position has not yet been filled.

III. CURRENT COMMERCIAL PRODUCT ACQUISITION POLICY EFFORTS

Although the history of the commercial product acquisition policy is instructive, the real issue before us today is the current status and future actions. As we have indicated, the Levin Legislation was principally responsible for an environmental change in support and consideration of commercial product acquisition issues. However, much remains to be done.

We continue to believe that support for a comprehensive commercial product procurement policy must come from the top policymakers at DOD, OFPP, and the other federal agencies. We can report that the individuals that occupy critical policymaking positions have given us the opportunity to express our views on actions that need to be taken. Their attention, and the attention of their staff, to these issues is absolutely critical.

At the same time, however, this issue needs to be raised on everyone's agenda. It would appear that while the top policymakers are in agreement that "something" needs to be done to encourage commercial product acquisition procedures, too little real action is occurring. Without the strong and active support of top procurement policymakers, field level procurement personnel will not take the initiative to identify and change those procurement practices that serve as real impediments to commercial companies doing business with the government.

Part of the problem is that most individual commercial product contracts involve relatively modest amounts of money when compared to major weapon systems and seldom involve controversial national security issues. As a result, while the squeaky wheels are getting the attention and grease, commercial product issues are too often ignored by top policymakers. This is the case despite the fact that commercial product contracts actually account for a very large number of the total transactions at DOD and elsewhere in the government.

Yet no single commercial product contract will ever create the need for immediate change. Rather, change must occur methodically and based on broad national policy issues of good government, increasing the strength of the national industrial base, increasing the competitiveness of commercial vendors, reducing government costs, and improving product quality. These are all issues that everyone cares about, but unfortunately are not attention grabbers.

Part of this problem is coordination and staff attention. Although the Office of the Secretary of Defense did assign one individual to be responsible for commercial product policy, little actual final work product and coordination has resulted from that position. In part, we believe this is because that single individual has been tasked to work on other "hotter" issues and has not been given the top level back-up necessary to coordinate with the Services and individual buying commands. As a result, while there is some positive activity taking place, it is disjointed and unorganized which dilutes any potential benefit to the taxpayer and seriously impedes the ability to increase commercial product acquisition.

IV. THE NEED FOR TRAINING

We are also concerned that too little has been done in the way of training government procurement personnel in the best methods to utilize commercial products. The sales forces of almost every commercial vendor regularly face government contracting officers and other procurement personnel that have been trained in and rely on a system designed to buy government-designed products from cost-based contractors. Without adequate training in buying commercial products using commercial-style procedures, many of the problems and cost-inefficiencies faced by both the government and commercial vendors will simply continue.

For example, when COMPACT first began to research these issues in 1985, we obtained a copy of a draft 1981 DOD manual on how to buy commercial products. That manual had never been finalized or distributed. Since that time there have been several unsuccessful attempts to update and finalize that manual while at the same time some of the services and buying commands have produced their own manuals. As training materials, manuals are, of course, the basic document and need to be revised on a regular basis as new techniques are discovered and unsuccessful techniques are discarded. This is especially true in the commercial products area where there is so little instruction and experience. By failing to distribute a comprehensive manual and be proliferating different manuals on the subject, DOD has made it more difficult to share ideas and quicken the education of all acquisition personnel.

V. EXISTING REGULATORY IMPEDIMENTS

As indicated, the environment is changing. Support for commercial product acquisition issues is growing. However, specific action is clearly required if we are to move beyond the "support" stage to the "action" stage. COMPACT has identified a number of actions that could be taken without a single law being written or amended. These actions can be accomplished by changes in current regulations and procedures.

A. Cost or Pricing Data Requests

Leading the list for needed regulatory changes is the need to solve the cost or pricing data problems that have become a nightmare of paperwork and endless negotiations for many commercial companies. What has happened in the cost or pricing area is that as the press, the Inspectors General, GAO, and Congress have all identified procurement decisions that were not made in the government's best interest, field level procurement personnel have reacted by becoming extremely cautious in their discretionary decision making and have seriously erred on the side of requiring as much information as possible in order to document all decisions made. Those information requirements, which often focus on cost or pricing data, serve only to increase the cost of doing business without any benefit accruing to the government.

The basic principal behind the requirement for cost or pricing data is and has always been that such data is sometimes needed to ensure the government receives a fair and reasonable price. This is especially true in a single source situation with a cost-based contractor. Contracting officers and the auditors that advise them, feel more comfortable with the traditional requests for cost or pricing data because it provides documentation for their acquisition decision should anyone care to ask. And because requiring cost or pricing data does not have any immediately noticeable effect on a commercial product price, it appears that it can be gathered for "free." The conclusion, therefore, of many contracting officers has been simply to require cost and pricing data in order to protect oneself.

Such requests for data and paperwork ignore the basic premise that fair and reasonable prices, can in fact, be obtained through a variety of methods such as competition, catalog pricing, historical pricing, and similar product pricing. This failure to utilize alternative means to ensure reasonable prices is a result, in part, from the serious lack of written guidance for purchasing commercial products and the lack of training in the proper use of cost or pricing data and the granting of exemptions.

For many contractors the submission of cost or pricing data is an almost impossible task. For example, the commercial accounting system for commercial vendors may not track all of the costs the government deems to be necessary under the definition of cost or pricing data nor do such systems track and segregate allowable costs from those costs deemed unallowable under federal cost principles. For large contractors with diverse operations and product lines, it is often very difficult, if not impossible, to track at a reasonable cost, all product costs at any particular time and associated with any particular product that could be sold to the government. This is particularly critical because the government wants "current" data and some commercial accounting systems simply do not provide ready access to such data because the commercial vendor has no need for it.

There is also the basic difference between cost-based government contractors and commercial vendors. Cost-based government contractors price their products based on estimated actual costs plus a profit. The commercial marketplace simply does not operate under those relatively simple procedures. Commercial companies make pricing decisions, not based entirely on costs and profits, but on intangibles such as product demand and marketplace competition. The often intangible nature of those pricing practices can vary from product to product and from company to company and would make it very difficult, if not impossible, to review and audit consistently those practices.

Companies unable or unwilling to submit cost or pricing data on demand have three basic choices: they can reject the government business; they can try to negotiate the request for cost or pricing data out of the contract or solicitation; or they can seek an exemption from submission of cost or pricing data. While the third choice is often the one selected by commercial vendors wanting to do business with the government, the standard exemption process has, itself, become a principle source of problems for the commercial vendor.

Pursuant to the current regulations, and with very little policy guidance outside of the Federal Acquisition regulation, exemptions to submitting cost or pricing data are granted after submission of the appropriate Standard Form 1412, Request for Exemption from Submission of Certified Cost or Pricing Data. The policy behind the SF 1412, like the policy behind cost or pricing data is reasonable; the government wants assurance that prices being charged are fair and reasonable. Unfortunately, the current system has lost sight of that policy and has focused instead on the very specific data requirements identified in the regulations in order to be granted a SF 1412 exemption.

The commercial marketplace does not always fit the narrow interpretations of the regulations. At the same time, contracting officers are fearful of being criticized for not getting enough data to document their decisions. As a result, contracting officers are requiring SF 1412s in inappropriate situations and do not use their discretion properly in granting exemptions where reasonable pricing is not the issue, but strict compliance with the existing regulatory tests is.

The confusion surrounding requests for cost or pricing data and the granting of exemptions can also have a more serious negative impact on commercial vendors. One commercial vendor that was involved in a dispute about the proper data required on a SF 1412 was threatened by the contract administration office with inclusion in the Contractor Improvement Program. The contract administration office sent notice of that fact to 30 of the commercial vendor's biggest government customers causing considerable confusion as to the vendor's status. A contractor placed in the Contractor Improvement Program faces possible debarment for failure to correct contract deficiencies. At the time of the dispute, the commercial vendor had not been awarded the contracts about which the data dispute centered. After numerous meetings and letters going back and forth, the contract administration office finally indicated that the contractor would not be placed in the program and agreed to review SF 1412s with similar data issues on a case by case basis.

As part of COMPACT's testimony before the Defense Science Board on June 16, 1988, COMPACT provided the Defense Science Board members with specific recommended changes in current regulations dealing with cost or pricing data. Those recommendations were also provided to the Director of the Defense Acquisition Regulatory System. The core of those recommendations were later adopted by and endorsed by the Council of Defense and Space Industry Associations and resubmitted to the DAR Council. It is our understanding that the Director of Cost, Pricing & Finance is currently reviewing those proposals at the request of the Deputy Assistant Secretary for Procurement. We look forward to having the opportunity to review those efforts.

The following are examples of situations where buying offices have unreasonably required cost or pricing data or a SF 1412 in order to grant an exemption from submission of cost or pricing data.

B. Products on the GSA Multiple Award Schedule

One method of selling commercial products to the government is through the General Services Administration's competitive Multiple Award Schedule Program whereby a potential contractor negotiates a volume discount with the government based on the total potential volume of sales. Once a product is on the schedule, agencies and authorized government contractors can directly purchase products, up to a certain Maximum Order Limitation. Congress has recognized the use of Multiple Award Schedules as a competitive process and included the Program in the definition of "competitive procedures" when the Competition in Contracting Act was enacted in 1984. See 10 U.S.C. § 2302(2)(c).

In negotiating schedule contracts, GSA obtains from potential contractors data that is similar to the type of data required on a SF 1412, only in much greater detail and vastly greater quantity. For example, GSA requires:

- o Certification that the product was developed without government funds;
- o Certification that the product is priced based on a catalog price with substantial quantities of the item having been sold to the general public at the catalog price; and
- o Current marketing information and discount data for the previous 12 months including: total annual sales to the federal government; total annual sales to non-government customers at catalog prices; total annual sales to non-government customers at other than catalog prices; the largest discount granted to a non-government customer; and the largest discount granted for quantities similar to the sales to the federal government.

The discount data is demanded, in various schedule programs, for all types of customer relationships, including those with dealers, distributors, and original equipment manufacturers, each of which represents a contractual relationship entirely different from that of the Schedule contract, where the government is simply an end-using customer. In some Schedule Programs, GSA even demands extensive data about other federal contracts, despite the fact that both statutes and regulations clearly state that the government is not a commercial customer.

This data is used to negotiate product prices and volume discounts. In order to ensure that the government receives the best possible prices, GSA wants to negotiate discounts calculated on total potential annual government volume of sales rather than the smaller number of products sold on each transaction. The final assurance given to the government in order to ensure a reasonable price is the inclusion of price reduction clause that guarantees the government the lowest price under the negotiated terms and conditions, even if prices are reduced after negotiations are concluded and the contract has been awarded.

All of this is required despite the fact that under a Schedule Contract, a vendor is not assured of selling even one item, or receiving a single dollar. The government actually refuses to make any contractual commitment of any kind; the Schedule Contract is nothing more than a granting of permission to sell. Even then, the Schedule contains a price reduction clause which has the contractual effect of indirectly regulating the competitive pricing discretion of commercial companies in commercial markets.

Commercial vendors continue to have serious concerns about the federal Multiple Award Schedule policy. In repeated submissions and public testimony commercial firms and trade associations, such a COMPACT, have identified current MAS policies as being a significant impediment to the entry of more commercial firms to the competitive government marketplace. It is a prime example of excessive regulation of the government contracting process involving commercial vendors.

Despite all of these protections, government procurement officers and in particular, prime government contractors continue to require SF 1412s for products on the federal supply schedules. For example, for one company, in Fiscal Year 1988, more than half all SF 1412s prepared were for products on the GSA schedule. Of that amount, the largest percentage of the requests came from government prime contractors responding to demands by government contract administrators.

Some effort has been made in the past by government procurement officials to both identify this as a problem and issue instructions indicating that SF 1412s were not necessary. These efforts have taken the form of:

o A 1983 Defense Acquisition Circular Number 76-42 that stated that a contracting officer "may dispense with the requirement" for the exemption form when ordering ADP equipment on the GSA schedule;
o A 1984 letter from the Assistant Deputy Under Secretary of Defense for Acquisition that indicated that the policy in DAC 76-42 remained in effect; and
o A 1986 letter again indicated that "contracting officer may dispense with the requirement for a SF Form 1412" when ordering an ADP item that is on the GSA schedule.

While these letters have been of some limited assistance when dealing with government contracting officers requesting SF 1412s for items on the federal supply schedules, the discretionary nature of the language and the limitation to ADP equipment have not solved the problem. In addition, as indicated by the requests from government contractors ordering Schedule products but still requiring SF 1412s, the letters have had little, if any, practical effect in actually changing policy or practice.

When faced with a request by a government procurement officer or a government contractor for cost or pricing data or a SF 1412, the commercial product vendor has three basic unenviable choices. The vendor can refuse the business, comply with the request, or attempt to negotiate with the contracting officer or buyer for the elimination of the requirement.

In a competitive marketplace it is, of course, difficult for a vendor to turn away sales and stay in business. This is particularly difficult when every effort is made to meet the needs of users and customers. Commercial vendors stay in business by meeting the needs of their customers. Refusal to meet those needs is a clear indication that the commercial vendor will not be around for long.

In order to comply with the request, the contractor faces the administrative burden of compiling the current and separate data for each SF 1412. This must be done carefully because of the nature of the certification that must be signed for each SF 1412.

The third choice, negotiating with the contracting officer, is almost always tried. Occasionally it works, it often does not. It is, however, always time consuming and administratively costly. Such negotiations can also create the false impression that a particular commercial vendor is difficult to deal with and one to be watched closely.

What is often the most frustrating is the conclusion of some contracting officers and government contractors that they are only following the regulations as they understand them. Because there is no clear guidance on this relatively simple matter, they refuse to go beyond a very narrow interpretation and simply demand cost or pricing data or the SF 1412.

The solution to this continuing problem should be simple. The Federal Acquisition Regulation should be amended so that neither the government nor prime contractors are to request SF 1412s for products on the federal supple schedules. This new regulation should be inserted at FAR Subpart 15.8 and should clearly set forth the policy in simple and direct terms. Such an amendment will not change government policy, only government practices. As such, it may be desirable to precede the actual FAR amendment with a formal policy letter from the new FAR Council explaining the policy on an interim basis.

This initiative will not increase the price for a single product sold to the government. It will not result in a single product being sold to the government at an unreasonable price. It will however, greatly simplify the acquisition process for many commercial vendors, it will decrease their cost of doing business with the government, and it will eliminate a continuing area of controversy between them and the government and government contractors.

C. Requirements for SF 1412s in Competitive Acquisitions

Another area of concern is the request for cost or pricing data or SF 1412s on a competitive acquisition. An elementary premise of contracting with the government is that fair and reasonable prices are obtained through competition. Indeed, the regulations clearly indicate that cost or pricing data should not be required when two or more responsive offers are received from responsible contractors.

Unfortunately, the perceived need by many government contract personnel to document every decision has led to a large number of requests for cost or pricing data or SF 1412s on acquisitions that are clearly competitive. Such a request places the commercial vendor in the same unenviable position of having to refuse the business, comply with the request, attempt to negotiate with the contracting officer and seek the elimination of the request, or submit a 1412 and request an exemption.

A particularly troublesome part of this problem involves government prime contractors that have been awarded a fixed-fee competitive government contract. In most cases, the prime government contractor was not required to submit cost or pricing data because the price for the contract was established as reasonable through competition. However, when those government prime contractors obtain commercial products from subcontractors, they often require the submission of cost or pricing data or SF 1412s for their files. It is important to note that such data is not being used to justify the fixed price the government is going to pay the prime contractor because that was set through competition. The data is demanded so that the prime contractor can respond positively to questions about obtaining cost or pricing data when their Contractor Purchasing System is audited by the government.

As example of this problem is evidenced by a recent major acquisition by the Army for computer systems and networking equipment. From the beginning it was clear that there would be numerous offerors responding to the solicitation in an intensely competitive field. Indeed, over 100 potential contractors attended the pre-solicitation conference.

The contract however, required the submission of cost or pricing data. When asked about this requirement in an obviously competitive acquisition, the contracting officer responded that cost or pricing data was required by the regulations for all contracts other than those based on cost or price only. Because this particular evaluation system also contemplated evaluating factors such as technical performance, logistics and support as well as price, it was the contracting officer's final opinion that cost or pricing data would have to be submitted. This action was taken in spite of a special May 1, 1987, memorandum from Deputy Assistant Secretary of Defense for Procurement Eleanor Spector to the Assistant Secretaries for each of the services and Directors of the defense agencies which indicated that as long as cost was weighted as 20 percent or more of the evaluation factors, adequate price competition existed.

This situation is actually quite common. One commercial vendor estimates that for every two requests they receive for cost or pricing data for which they submit a SF 1412, they receive a third request for cost or pricing data which is eventually dropped after negotiations with the contracting officer. This is particularly a problem for small businesses that do not have the resources or staff to dedicate to negotiate repeatedly.

Once again the solution is relatively simple. The Federal Acquisition Regulation must be amended to set forth clearly the policy that cost or pricing data simply is not be requested when competitive acquisitions are used. Such regulations need to be expressly extended to government prime contractors so as to meet their needs in dealing with federal auditors.

D. Requirements for SF 1412s - Previous Large Government Purchase

When buying commercial products at fair and reasonable prices, the current regulations for exemption from submitting cost or pricing data do not take into account the effect that a single large government purchase during a particular accounting period can have on the data submitted on a SF 1412 to the government. Under the current regulations, strictly enforced by contracting officers everywhere, government sales of a product cannot account for more than 65 percent of the product sales without requiring cost or pricing data.

Under regular circumstances, a commercial vendor rarely has difficulty in meeting this criteria. However, should a government buying office come in and buy a large number of a particular product, an exemption from cost or pricing data is granted for that acquisition, but for future acquisitions, the commercial vendor may not be able to meet the exemption criteria because the large government purchase has skewed the percent of sales test.

For example, one commercial vendor had a request for exemption rejected by the Navy because the Army had recently purchased a large number of the same commercial product. Prior to the Army purchase, government sales during the relevant time period represented less than 9 percent of the product sales. After the Army purchase, government sales represented over 56 percent of the product sales. In order to be granted the exemption, the commercial vendor had to submit data for a two year period, which was collected at considerable expense. As a result, a situation is created where the commercial vendor has not changed its prices and is willing to sell its products to the government at the prices it charges everyone else and previously considered fair and reasonable by the government. Nevertheless, contracting officers and auditors demand cost or pricing data and for some commercial vendors refuse to grant exemptions or otherwise unreasonably delay procurements.

E. Requirements for SF 1412s - New Products

A similar problem occurs when a new product is introduced by a commercial vendor. In the electronics marketplace, commercial vendors face the task of constantly developing and adopting new technology in their products. Failure to do so means that in just a year or two, an entire generation of developments can occur and a former market leader can find itself out of the market completely.

As stated above, however, under the current regulations, in order to receive an exemption from submission of cost or pricing data, government sales may not account for more than 65 percent of the sales of a product. The government on the other hand, often wants to buy a commercial vendor's newest product with the latest technology. And the government can demand, through the use of the Defense Priority Allocation System, that it receive delivery prior to other customers. The result is, of course, that for initial introductory periods, the government is the first significant purchaser and the commercial vendor is unable to meet the percentage of sales test in the regulations for exemption from cost or pricing data.

For example, one commercial vendor, in response to a competitive, two-step invitation for bids, originally submitted an "A" version of a product. Toward the end of the bid sample evaluation process, the commercial vendor notified the contracting agency that the products it submitted as bid samples were being commercially upgraded to take advantage of the latest technology. The commercial vendor offered to substitute the newer model. The contracting agency evaluated the new models and approved the substitution. This assured the contracting agency would receive products at the same advanced technical level as the vendor's commercial customers.

At the conclusion of the qualification period, the contracting agency notified the commercial vendor that the solicitation was being converted into a single source, negotiated acquisition, citing lack of competition. After submission of a proposal by the commercial vendor, the contracting agency asked for cost or pricing data to support the prices offered. This request for cost or pricing data began a year and a half of paperwork, audits, meetings, letters, telephone calls, submissions, and clarifications. During that time, there was never any question that the prices were not fair and reasonable, but concerns and complaints by the administrative office assisting the contracting agency about the supporting data prevented the award from being made. During this period the government users were denied access to urgently needed products for an unacceptable period of time.

In order to show substantial sales to the general public of the new products, the commercial vendor had to convince the contracting agency to accept sales data based on sales of the earlier models of the items being offered. The government was to be the first substantial purchaser of the new models because introduction of those models into the commercial marketplace was scheduled for a later date.

By the time all issues were finally resolved, the new models were in commercial production. The government then advised the commercial vendor that the original request for exemption from submission of cost or pricing data had expired and a new request for exemption had to be submitted. Revised sales data based on sales of the new models were submitted twice. The first revision included sales covering the first three months of commercial production. The quantities sold during the first three months were deemed too low by the administrative agency to grant an exemption. Nearly four months later, a second revision, based on seven months of commercial sales was submitted. By that time the commercial vendor was able to demonstrate substantial sales to the general public by virtue of the fact it was shipping the products out the door to everyone but the contracting agency. The government finally accepted the sales data and granted the exemption.

F. Requirements for SF 1412s - Spare and Replacement Parts

A similar problem is faced when the government wants to buy spare parts for commercial products. Unlike commercial customers that take advantage of commercial worldwide distribution and maintenance operations, the government has concluded it needs to provision for commercial products in the same way it provisions for tanks and other weapon systems. In addition, the government often buys spare parts for electronic equipment at the more costly assembly level rather than the lower cost component level, as is the practice with commercial customers.

Putting aside for the moment the discussion as to whether the government should be spending money on this type of provisioning, it does create significant administrative problems for commercial vendors. Prices for spare parts for instruments are often sold by necessity on a single source basis, almost always at catalog prices. As a result, the government wants cost or pricing data or the contractor must submit a SF 1412 request for exemption. For those parts that commercial customers buy, the government is willing to approve a request for an exemption from submitting cost or pricing data. However, for those parts purchased almost exclusively by the government, either because they never wear out so commercial customers never buy them or because they consist of entire assemblies that commercial customers do not buy, commercial vendors often due not have the sales data sufficient to meet the current strictly enforced regulatory tests for granting an exemption from submission of cost or pricing data.

Again, considerable time is spent negotiating with the government for a way around this apparent roadblock. One of the more creative solutions to this type of impasse involved having a commercial vendor sell extra complete instruments to the government, with the requirement that the commercial products were to be shipped unassembled.

COMPACT wants to emphasize that seldom if ever is there a discussion about whether our price is reasonable or unreasonable. All of the discussions, negotiations, correspondence and paperwork focus almost exclusively on meeting someone's strict interpretation of current regulations applicable to granting exemptions from submission of cost or pricing data.

G. Evaluation Factors - Costs of Ownership and Quality Costs

A fundamental difference between the government marketplace and commercial practices is the factors evaluated when a purchase decision is made. While the government marketplace, when buying commercial products, relies almost entirely on initial product price, the commercial marketplace relies not only on initial product price, but on the other costs of ownership and quality costs factors such as reliability and maintainability.

As more and more acquisitions have been found to be faulty by internal and external investigations, contracting officers and other government contract personnel have retreated to evaluating products on the single factor that is most easily quantifiable, initial or instant product price. No one has ever been publicly criticized for buying the lowest priced product if it met the stated minimal specifications. However, as the commercial marketplace practices indicate, the lowest initial or instant product price does not always translate into the lowest total overall cost. Indeed, many large commercial vendors stay in business because their products represent the best overall buying decision at reasonable and competitive, but not necessarily the lowest, prices based on life-cycle costs and other related factors.

In recognition of these facts, the U.S. Army Communications Electronic Command at Fort Monmouth, N.J. has recently instituted a Blue Ribbon Contractors program that recognizes both past quality and delivery performance as factors of importance to the Army. As indicated in the April 14 1989, letter to potential contractors, CECOM contracting officers may award a contract to a Blue Ribbon contractor at a price up to 10 percent higher than the low offeror.

The program is open to all contractors selling products in a number of specific federal supply classes including:

6140 - Storage Batteries
5960 - Electron Tubes
6625 - Meters

5805 - Telephone and Telegraph Equipment
5965 - Headsets, Handsets, Microphones and Speakers
6740 - Photographic Developing and Finishing Equipment
5810 - Communications Security Equipment and Components
5815 - Teletype and Facsimile Equipment
5920 - Radio and Television Communications Equipment

Before the Program is applied, at least two Blue Ribbon Contractor for any one federal supply class must be approved.

In order to qualify as a Blue Ribbon Contractor, the commercial vendor must sell one of the listed products and must meet critical, objective criteria. The commercial vendor must have a demonstrated 90 percent or higher on-time delivery on CECOM contracts in a given supply class during the past 12 months. In addition, the contractor must have demonstrated quality performance as indicated by Quality Deficient Reports which are defined as a report due to a defect found during acceptance or visual inspection or during functional test or checkout which indicates a failure or that failure is imminent. In order to qualify, a contractor cannot receive more than one Quality Deficiency Report on contracts worth up to $50,000; no more than two on contracts between $50,000 and $500,000, and no more than three on contracts over $500,000. The contractor also cannot have any known in-plant quality system problems.

Although this system is not perfect, it does achieve two very important goals: (1) it recognizes that lowest initial product price is not the only factor that is of importance to the government and (2) it permits a simple objective quantification of two other-than-price factors for purposes of comparing products and awarding contracts. We would expect that as CECOM contracting officials obtain more practice and information with the Blue Ribbon program, refinements can be made to make it a more exacting tool. We would also like to see the program extended to more commercial products.

It is important to note that programs such as the Blue Ribbon Contractors program should be encouraged at buying commands through DOD and the federal government. Such programs will increase the experience of evaluating products based on total costs of ownership and quality costs factors and will assist in providing the collective knowledge necessary to make improvements. It should be remembered and recognized that no system is perfect. We suspect that mistakes will be made. Chances are, however, that fewer overall mistakes will be made, and as contracting officers become more accustomed to evaluating total costs of ownership and quality costs, the greater the likelihood that products will be purchased that actually do represent the lowest total overall cost to the government.

H. Flow-Down Clauses

As indicated above, commercial vendors face additional problems related to the manner in which the government does business when contracting with prime government contractors. The prime contractors, following government requirements and demands insert into subcontracts numerous government clauses and requirements that increase the cost of doing business with little if any benefit accruing to the government. The following is a typical example of the type of paperwork that occurs under such a system.

A Prime Contractor wanted to buy two, handhold multimeters as part of the ground support system for a particular airplane. The multimeters, part of the commercial vendor's regular catalog pricing, sold for $199 each.

The Prime Contractor originally telecopied the first two pages of the Request for Quotation to the commercial vendor and sent the rest by mail "due to the size of the Logistics Statement of Work." Under the solicitation, the commercial vendor would have had to commit to:

a. Ensuring an inspection system in accordance with MIL-I-45208, MIL-C-45662 and/or MIL-Q-9858;
b. Identifying nonrecurring elements of cost;
c. Supplying the product under the DPAS order system;
d. Submitting cost or pricing data;
e. Giving the Prime Contractor access to cost records;
f. Marking the items pursuant to MIL-STD-130;
g. Agreeing to the special warranty terms as described in the Statement of Work;
h. Following the technical requirements of the Statement of Work;
i. Providing the Prime Contractor with plant inspection rights;
j. Providing written certification that the device has been proof load tested to 200 percent of its rated working capacity;
k. Complying with several pages of fine print and contract clauses, some of which add additional military specifications requirements, others that repeat requirements for cost or pricing data, and others that are simply not applicable; and
l. Providing supplier test results.

The commercial vendor originally responded to the Prime Contractor by letter of May 6, 1987, indicating it would be willing to sell the two items for $378.10. The commercial vendor also suggested that the Prime Contractor could purchase the parts from an authorized dealer or off the GSA schedule. The commercial vendor took exception to the Prime Contractor's contract terms and conditions.

By letter of June 22, 1987, the Prime Contractor notified the commercial vendor that although the original Request for Quote was sent based on the assumption that "commercial standards" would be applicable, further review indicated that all support equipment would have to be purchased to "government standards." The Prime Contractor then added and deleted various clauses, including "Additional Terms and Conditions - Government" which included Technical Data rights clauses and various certifications.

By letter of June 26, 1987, the Prime Contractor notified the commercial vendor that "[d]ue to the documentation involved..." the due date was to be extended. By letter of July 21, 1987, the commercial vendor again indicated that they would not be responding because it is not "cost-effective for [the commercial vendor] to invest the time and resources necessary to respond fully to the requirements..."

By letter of July 22, 1987, the Prime Contractor notified the commercial vendor that the commercial vendor needed to extend its offer through October 30, 1987. The sale was never made.

This example shows the extremes that Prime Contractors will go to follow government instructions when contracting with others. The commercial vendor faces the same choices as in dealing with the government when unreasonable and burdensome requests are made: (1) reject the work; (2) comply; (3) attempt to negotiate a reasonable solution.

I. Standard Form Government Contract For Commercial Products

In order for the government to implement more commercial-style procedures as recommended by the Packard Commission, the contract instrument must be significantly amended. COMPACT's analysis of just seven contracts for commercial products indicated:

- 170 FAR Clauses that were incorporated by reference or in full text in at least one of the contracts;

- 53 DFAR Clauses that were incorporated by reference or in full text in at least one of the contracts: and

- 34 Other FAR Supplements Clauses promulgated by individual buying commands that were incorporated by reference or in full text in at least one of the contracts.

The plethora of clauses and their inappropriate use make it significantly more difficult to do business with the government as a commercial vendor. In particular, oftentimes the process specifications incorporated into a contract are out of date. For example, in the electronics field, a specification for Electro Magnetic Interference (EMI) is often inserted into contracts. The specification is MIL-STD-461. However, there are at least three version of MIL-STD-461 that are currently used by the government including MIL-STD-461A Notice 4 dated February 9, 1971; MIL-STD-461B dated April 1, 1980; and MIL-STD-461C dated August 4, 1986. The older versions of a specification can refer to other out-dated specifications that in turn refer to specific test equipment that is no longer in production. As a result, certain tests cannot be performed unless the obsolete equipment can be found.

The inappropriate use of clauses also requires the commercial vendor to dedicate time to negotiating with the contracting officer for the removal of such clauses. For example, a commercial vendor must take exception to clauses routinely incorporated into contracts including:

- Configuration Control - Engineering Changes, Deviations, and Waivers;
- Cost Accounting Standards;
- Identification of Sources of Supply;
- Identification of Expenditures in the United States;
- Higher-Level Contract Quality Requirement; and
- Certification of Commercial Pricing;

These problems are especially significant for the small businesses that are unable to afford full-time government contract specialists to review the extensive clauses and requirements as well as for the large business that must deal with hundreds of different buying offices and hundreds of different contracts and requirements.

COMPACT strongly recommends that the government begin the process of adopting a standard form government contract for commercial products. Such a contract could be drafted that complies with all current statutory requirements and yet significantly reduces the number and type of clauses routinely used in contracts for commercial products.

COMPACT recognizes that there will always be differences between government contracting and commercial marketplace contracting. However, the goal should be to eliminate as many differences as possible and to create a document with standard clauses and requirements. Such a document would eliminate one of the significant barriers to entry to the government marketplace for many businesses by reducing the administrative costs involved in reviewing individual contract terms and conditions, reducing the risk of doing business with the government, and eliminating the need to negotiate for the removal of inapplicable clauses.

J. Government Inspection and Quality Assurance

Another area of concern for commercial vendors is the current requirements for government source inspection and the use of commercial warranties. Commercial companies spend a significant amount of time and effort satisfying the quality demands of its commercial customers, both domestic and international. Those companies failing to satisfy the buyer do not exist for long.

At the same time, the documentation requirements demanded by government specifications and standards add significantly to the cost of doing business with the government without adding quality. Those documents and procedures are often out of step with the advances made by industry with regard to quality control and assurance. Documentation by itself does not produce quality.

One COMPACT member, a worldwide leader in quality control, absorbs an estimated $150,000 a year administering orders where government inspection and associated DD-250 Material Inspection and Receiving Reports are required. In addition, the commercial vendor also provides office space and facilities for a government inspector who spends 2 to 3 days a week reviewing the commercial company's processes or performing physical inspections. The rest of the time is spent by the inspector with other firms in the geographical area with DOD contracts.

This process and the associated paperwork is completely redundant to commercial vendor's quality control process and often results in payment being withheld by the government for the slightest typing errors. More importantly, no added benefit or improved quality is achieved because of the government inspection process. The inspection resources would be better spent on firms involved in critical, noncommercial products and with those firms that may have little or no experience in the product field for which they have a contract.

The government should rely on a company's quality control system for non-critical commercial products, unless a significant problem arises. Otherwise, the government source inspection should be limited to mission critical, life or health threatening situations. If a problem does arise, then the commercial vendor should have to work very hard to eliminate strict inspection requirements and gain back its reputation as a responsible, quality conscious vendor.

The Civilian Agency Acquisition Council and the Defense Acquisition Regulatory Council have recently recognized that commercial vendors must do a good job of quality control in order to satisfy commercial customer and remain in business. As a result they have recommended a change in FAR that would permit the use of the commercial vendor inspection of supplies clause rather than government inspection. COMPACT strongly endorses this concept.

Protection for the government is based on the reputation of the commercial vendor and the commercial warranty given with the item being purchased. For many products, commercial warranties range from 90 days to 3 years, with 1 year being standard. The commercial marketplace uses the warranty period to ensure itself that the product works as it was intended. We note with some concern, however, that many government agencies, and in particular DOD, have chosen not to use commercial warranty provisions obtained when a commercial product is purchased.

For quality commercial vendors, warranty work increases only slightly the manufacturer's costs for a particular product. Quality commercial vendors encourage the use of warranty provisions for several reasons. First, warranty work provides the commercial vendor with critical data about product failures and the need to make system or design improvements. Without such data from all types of users, potential problems could go uncorrected.

Second, commercial vendors have the properly maintained capital equipment necessary to diagnose and repair faulty products. In the electronics industry, much of the test equipment is sensitive, expensive, and complex. The commercial vendor is in the best position to make sure that such equipment is maintained properly and utilized at rates that are cost-effective.

Third, commercial vendors have properly trained and highly skilled personnel enabling them to perform quality repair work resulting in a more accurate repair. The government oftentimes requires the commercial vendor to prepare special repair manuals to be written at a 9th grade level to be used by less skilled technicians working on equipment worth tens of thousands of dollars. The opportunity for error or an incorrect repair is less likely where the repair technicians are highly trained. This also helps assure that only properly repaired products are returned to the field

Fourth, the commercial repair facility can complete the repair more quickly resulting in less downtime and an increase in user satisfaction. This is a result of the combination of having the appropriate and properly maintained capital equipment, properly trained technicians, and readily available replacement parts. This ensure a rapid turnaround time for the product. It also allows the commercial vendor to upgrade the product by replacing potentially defective parts or substituting existing parts with newly designed parts at little or no extra cost.

Finally, commercial vendors recognize the opportunity for additional business beyond the warranty period. A principle part of the entire concept of buying commercial products in a commercial-like manner is taking advantage of the services offered by commercial vendors when it is cost-effective. All too often in the government marketplace, initial procurement decisions are made separately from operation and maintenance decisions. Commercial customers recognize the value of follow-up services provided on a world-wide basis and evaluate those costs when making a purchase.

We would encourage acquisition officials to consider and take advantage of commercial warranties when determining the lowest overall cost to the government.

K. Defense Priorities And Allocations System

An additional problem facing commercial vendors when doing business with DOD is the universal use of the Defense Priorities and Allocation System (DPAS). Section 2071 of 50 U.S.C. APP. authorizes the President:

> to require that performance under contracts or orders ...which he deems necessary or appropriate to promote the national defense shall take priority over performance under any other contract or order, and for the purpose of assuring such priority, to require acceptance and performance of such contracts or orders by any person he finds to be capable of their performance....

The regulatory implementation of this statute, given to the Department of Commerce, provides only general guidance and does not contain a provision for ensuring that the DPAS rating is used only when it actually is "necessary or appropriate to promote the national defense...."

For commercial vendors, DPAS rated orders require special systems that trace material requirements; special systems for flowing down ratings to subcontractors; the ability to shift production schedules; and too often causes delay in deliveries to commercial customers. These systems and changes are necessary even though the DPAS rated commercial product may not be needed by DOD on a priority basis and often ends up in a storage depot after shipment.

We believe it is fair to say that commercial vendors are more than willing to do their part to assist in the promotion of national defense. However, the indiscriminate use of such priority ratings on nearly all DOD orders is an abuse of the system and a costly impediment to doing business with the government. Greater instruction on the proper use and an occasional audit of the DPAS ratings would go a long way to eliminating this particular impediment.

VI. RECOMMENDATIONS

COMPACT appreciates the effort and interest of the Subcommittee in evaluating the efforts to implement a comprehensive commercial product acquisition policy in the government. Since the enactment of the Levin legislation, we have witnessed a clear improvement in the environment for accepting the value and benefits of commercial products by government procurement personnel. However, that environment can quickly turn cold again if policy is not converted into action and changes. In order to achieve the fundamental policy provided for in the Levin legislation and the recommendations of the Packard Commission, COMPACT recommends that the following actions be taken:

o Develop and initiate training programs in commercial product acquisition techniques that cover: market research techniques; commercial product pricing policies; the proper, limited use of cost or pricing data; the proper means of granting exemptions to the submission of cost or pricing data; and the use of commercial-style practices;

o Issue a policy letter as soon as possible that clearly indicates that SF 1412s shall not be requested for commercial products that are also sold on the GSA Multiple Award Schedule; the policy letter should be applicable to government contracting personnel as well as prime government contractors doing business with commercial vendors as subcontractors on government contracts.

o Amend FAR Subpart 15.8 so that SF 1412s shall not be requested for commercial products that are also sold on the GSA Multiple Award Schedule; the regulations should be clearly applicable to government contracting personnel as well as prime government contractors doing business with commercial vendors as subcontractors on government contracts.

o Amend FAR Subpart 15.8 to include language changes as recommended by COMPACT in its submission to the Defense Science Board and the submission by the Council of Defense and Space Industry Associations so as to provide clear guidance for eliminating unnecessary requests for cost or pricing data and properly granting exceptions.

o Require the use of a standard form government contract for commercial products that relies to the maximum practicable extent on commercial terms and conditions.

o Establish a system whereby standard commercial warranties are utilized to repair and maintain commercial products.

o Amend the Defense Priorities and Allocations System regulations so that a DPAS rating is used only when justified by national defense needs.

TESTIMONY OF

JOHN McGOWAN
FEDERAL PROCUREMENTS MANAGER
HEWLETT-PACKARD COMPANY

Mr. Chairman, Members of the Subcommittee, my name is John McGowan. I am the Federal Procurements Manager for the Hewlett-Packard Company. As you may know, Hewlett-Packard manufactures and distributes a wide range of electronic products from electronic test and measurement equipment to computers to health care equipment. Last year we had total sales of about $10 billion. Of that, about 4 percent was in sales to the federal government and about 2 percent was in sales to federal government prime contractors. In my position as Federal Procurements Manager I am responsible for all of our federal sales policies, the functional management of federal proposal preparation and contracts administration as well as providing training and support systems for our federal marketing and contract efforts.

I very much appreciate the opportunity to testify before you today. Hewlett-Packard and its Chairman, David Packard, are particularly interested in trying to improve the current federal acquisition system and to see implemented an improved comprehensive commercial product acquisition policy. Like the other COMPACT members, Hewlett-Packard shares a concern that while a lot of attention and effort have been focused on acquisition problems over the past several years, too little effort has been focused on taking advantage of commercial products and commercial practices.

Cost or Pricing Data

Of the many existing impediments that a commercial product vendor wanting to do business with the government must face, one of the most significant, as indicated in COMPACT's written testimony, is the number of incessant requests for cost or pricing data. Serious problems are encountered in attempting to do business with the government involving new product offerings or products which have been modified to meet a special government need. Too often the government's only contractual solution is to demand cost and pricing data. When a commercial firm such as ours is unwilling to do business in that way, an insoluble impasse results. There must be meaningful reform of the government's regulatory policies if these types of impediments to the acquisition of commercial products are to be removed. Clearly, unnecessary and inappropriate federal demands for cost and pricing data represent a significant problem and one that must be resolved. I would like to address two aspects of that problem this morning.

First, we are continually faced with the need to submit a request for exemption from the submission of cost or pricing data, a SF 1412 for products that are on the General Services Administration Multiple Award Schedule. According to company data, we prepared almost 500 of these last year.

What is particularly troubling about these requests for cost pricing data or SF 1412s is the fact that Congress specifically recognized federal supply schedules as a competitive procedure when it enacted the Competition in Contracting Act in 1984. Despite this clear recognition of its competitive status, government contracting personnel and government prime contractors often require a certified SF 1412 prior to buying a product that is listed on a federal supply schedule. Although we are sometimes able to eliminate these requests through negotiations, more often than not, the contracting officer or buyer advises us that the SF 1412 is to be provided or no contract or subcontract will be awarded.

As a result, Hewlett-Packard must gather and document recent commercial sales data for certification of commerciality in each of these government sales. I should point out that this data is similar and in many cases identical to the data that was provided to GSA or certified to when commerciality was established at the time that the GSA schedule was negotiated. In addition, GSA negotiates its contracts and discounts based on the expected total annual sales by product group to the government, so the price offered is, in fact reasonable, based on aggregate volumes. I would add that none of the SF 1412's prepared for products on GAS schedules have been rejected after review by the auditors.

A related problem involves requests for cost or pricing data in solicitations that are clearly competitive. The purpose, of course, of obtaining cost or pricing data is to ensure that prices paid are reasonable. The current regulations indicate that cost or pricing data should not be required where adequate price competition exists and reasonable prices are therefore obtained.

Despite this relatively clear regulatory guidance, contracting officers, for reasons we don't understand, frequently demand cost or pricing data even when robust, full and open competitive procedures are being utilized. For example, in one recent military procurement for Computers and Communications Equipment, over 100 companies attended the pre-solicitation bidders' conference. Yet, in a clearly competitive situation, the contracting officer demanded cost or pricing data. When asked to explain his reasoning, the contracting officer stated that his interpretation of the regulations indicated that cost or pricing data was required for all contracts where price was not the sole evaluation factor. And because the current solicitation indicated that technical performance, logistics and support, as well as price were to be evaluated, price competition did not exist. This interpretation of the regulations even contradicted written policy guidance by the Deputy Assistant Secretary of Defense for Procurement indicating that price competition exists as long as price accounts for 20 percent of the evaluation criteria. Based on his own interpretation, the contracting officer refused to eliminate the cost or pricing data requirement.

Even if this particular contracting officer had finally eliminated the cost or pricing data requirement, the process has a significant and costly flaw in it. That flaw is the need for companies constantly to negotiate with contracting officers about regulatory requirements involving cost or pricing data. We estimate that for every two requests for cost or pricing data under which we submit a request for exemption by compiling and submitting a SF 1412, we receive a third such demand which is ultimately eliminated through negotiation. That process is costly for us and requires us to maintain full-time staff to prepare and support the audits of these certifications. In addition, much time is spent training and negotiating with employees and customers over the requirements of these requests.

Evaluation Factors - Quality Costs

An additional area of concern is the manner in which the government evaluates the lowest total overall cost of a particular commercial product. The concept of "lowest total overall cost" is the maximum of the law, and is, in fact, *not* inconsistent with buying decisions in the commercial business world. In the commercial marketplace, buyers evaluate products based not only on the initial or instant product price but also on the basis of long term quality cost factors such as reliability and maintainability. However, as federal procurement has become more and more controversial over time, government contracting officers have retreated to evaluating commercial products on the single factor that is most easily quantifiable, the initial or instant product price. Even when quality cost factors are officially included in procurements they are too often treated in a pass/fail fashion, with the final decision based strictly on the lowest instant price.

Recognizing that it is not always in the best interest of the government to make acquisition decisions based entirely on initial product price, a few buying commands have now instituted experimental or trial" programs. We are familiar with the operation of a program operated at the U.S. Army Communications Electronic Command at Fort Monmouth, N.J., called the "Blue Ribbon Contract" program. The Army objectively evaluates contractors on past product quality and delivery performance. The program permits a contracting officer to award a contract to a certified Blue Ribbon Contractor as long as the product price is within 10 percent of the lowest offered product price. A higher differential may be permitted if approved by the Director or Deputy Director of Procurement.

This effort is an excellent start at trying to recognize and evaluate the genuine total costs associated with the life cycle of any particular product. Such efforts need to be encouraged at buying offices throughout the government. In addition the lessons learned from those programs need to be collected and evaluated so that the programs and evaluation processes can be constantly improved.

We note that when COMPACT was first getting organized back in 1985, we spoke with Professor John Cibinic of the National Law Center at George Washington University. Professor Cibinic is recognized as one of the leaders in the area of government contract law and policy development. Professor Cibinic indicated almost four years ago that what the government needed to do to implement a comprehensive commercial product acquisition policy was to begin trying various innovative acquisition procedures that copied commercial practices. He was convinced then, as we are now, that although the government might make some mistakes, the lessons learned would be far more valuable than additional studies and reports about the policy itself. We view the Blue Ribbon Contracting Program as just such an effort and one that needs to be expanded.

Let me conclude by again stating that we appreciate your attention to these issues. These issues will never be as exciting to the public as a multi-billion dollar weapon system that doesn't work, but at the same time, the solutions to these problems will go a long way toward deriving the full benefit of competition in the government contracting by ensuring that the additional costs of doing business with government are kept to a minimum, and impediments are removed, thus bringing more commercial suppliers into the competitive process.

I would be pleased to answer any questions you might have.

TESTIMONY OF
AL HERMAN
GENERAL MANAGER
FEDERAL SYSTEMS DIVISION
TEKTRONIX, INC.

Mr. Chairman, Members of the Subcommittee, my name is Al Herman. I am General Manager of the Federal Systems Division of Tektronix, Inc., located near Portland, Oregon. Tektronix is an electronics manufacturer of commercial off-the-shelf design, test, graphics, and communications products. Last year Tektronix's consolidated sales were slightly over 1.4 billion dollars. Direct sales to the U.S. Government were 9% of consolidated sales or about 125 million dollars. In my position as General Manager, I am responsible for sales and sales support of 80 million dollars of commercial products to the U.S. government - primarily the military services. This includes responsibility for marketing, order processing, accounting, contract negotiations and logistics support. In addition, I am responsible for Tektronix's cost-based sales to the government which will be about 5 million dollars this year.

I want to begin by thanking you for the opportunity to testify before you today. Tektronix, a COMPACT member, has been an active participant in helping to identify the specific government procurement impediments our industry faces. We have worked equally hard, with the other members, to recommend solutions. The rapidly changing and expanding body of government procurement statutes, regulations and oversight activities have a major effect on commercial vendors such as ourselves -- companies whose businesses must operate in a highly competitive commercial international marketplace. The acquisition system may be changing for the better in its increased ability to control the cost-based business of the noncommercial defense contractor, but the complex controls involved are often inappropriate for the commercial off-the-shelf product industry. We are being held to strict interpretations of regulations which I believe provide marginal or no benefit to the government for procuring commercial off-the-shelf products. And both industry and the taxpayers must absorb the costs these regulations unnecessarily produce. We are also aware that many companies avoid government business, concerned with adverse publicity, the information and documentation and certification requirements, a host of compliance issues, disruptive audits and investigations and the unreasonably massive liabilities for errors.

Cost or Pricing Data

Our current primary concern involves requests for cost or pricing data for commercial off-the-shelf products. Like most other commercial vendors, Tektronix relies on a commercial accounting system designed and scaled to satisfy our commercial needs. Such systems are of the absolute minimum size and scope necessary to ensure that business can be conducted responsibly and that appropriate reports can be provided to managers, shareholders, and others. Commercial vendors simply cannot afford to develop and maintain the elaborate accounting systems required of the cost-based government contractors. Our ability to compete successfully in the intensely competitive commercial electronics markets depends upon our ability to operate at costs comparable to those of our international competitors.

We necessarily rely upon a market-driven catalog pricing system. Our prices are based upon a number of factors. But to a great extent, they are driven by the supply and demand fundamentals which are the basis of our successful national economic system. In other words, the marketplace determines their fairness and reasonability. Despite our commercial pricing program, under the current cost or pricing regulations, and perhaps even more importantly, under the increasingly stringent interpretations of individual contracting officers, we often receive requests for cost or pricing data on acquisitions of commercial products where the government clearly is protected from unreasonable pricing

For example, Tektronix recently responded to two solicitations for specialized cable test products. These particular solicitations required the submittal of sample instruments so the agency could test them and ensure their needs would truly be met. Vendors whose products passed the test would then be solicited on a competitive basis. The products Tektronix submitted were current catalog items, but were soon to be replaced commercially by upgraded versions. Although the upgraded products were not yet being shipped to the commercial public, they were nevertheless offered to the agency, who tested and agreed to accept them.

As it turned out, no other vendor's product passed the test requirements of either solicitation. Because there was no other competing vendor, the solicitation was converted from a competitive sealed bid to a single source negotiated RFP requiring cost or pricing data.

Since the products were commercial and Tektronix could not provide cost or pricing data, we requested an exemption. In order to show substantial sales to the general public of the new products, Tektronix had to convince the contracting agency to accept sales data based on sales of the earlier submitted versions of the items being offered. The agency would be the first substantial purchaser of these new items because introduction into the commercial marketplace was not scheduled until late in 1987.

Tektronix, during this period, also had to convince the government to recognize that a recent, large government buy of one of the prior products had skewed sales data to the extent that it fell in the gray area for qualifying for an exemption from cost or pricing data submission. However, by examining two years worth of data and by comparing the sales data of the sold at catalog prices in substantial numbers to the general public, and the government finally accepted the sales data.

By the time all issues were finally resolved with regard to pricing of the spares and technical data, the new versions were in commercial production. The government then advised Tektronix that the originally submitted request for exemption had expired and a new claim for exemption was required. Revised sales data based on sales of the new models was submitted twice. The first revision included sales covering the first three months of commercial production. The quantities sold during the first three months were deemed too low by the administrative agency to grant an exemption. Nearly four months later, a second revision, based on seven months of commercial sales, was submitted. By this time Tektronix was able to demonstrate substantial sales to the general public by virtue of the fact it was shipping the products out the door to everyone but the contracting agency who needed them. The government finally accepted the sales data and granted the exemption a year and a half later.

To give you an idea of the amount of effort that went into this process I have brought with me a box containing the correspondence and data which was necessary to support our offer. A similar sale to a commercial customer would have required perhaps a few pages of documentation.

A related problem occurs when the government wants to buy spare parts for commercial products. Unlike our commercial customers who take advantage of Tektronix's worldwide distribution and maintenance operations, some agencies of the government have concluded that they need to provision for commercial products in the same way they provision for tanks and weapon systems. To facilitate their need to service their own equipment, they buy spare parts for electronic equipment at the assembly level rather than the component level. This simple change creates significant administrative problems for commercial vendors. Spare parts for commercial products are often available only from the manufacturer, but almost always at established and published catalog prices. In the absence of competition, the government requires the contractor to submit cost or pricing data or a SF1412 request for exemption. For those parts that commercial customers routinely buy, the government is willing to approve a request for an exemption from the submittal of cost or pricing data, but only _if_ the sales are substantial, a term subject to varying interpretations by different government entities. Some parts, particularly the assemblies mentioned above, are purchased almost exclusively by the government. Therefore, we often do not have commercial sales sufficient to meet strictly enforced regulatory tests for receiving an exemption from submission of cost or pricing data for spare parts.

Again, considerable time (measured in months and years) is spent negotiating with the government for a way around this roadblock even though there is no question regarding the commerciality of the products for which the spares are being purchased or the fairness of the price of the spare parts. Agencies have even considered buying extra complete products, which we would ship unassembled for their parts. Procuring agencies are caught in these regulations just as the contractors are. But most contracting officers are reluctant to seek innovative solutions in the current procurement climate.

I want to emphasize that seldom, if ever, is there a discussion about whether the prices being offered by off-the-shelf commercial vendors is reasonable or unreasonable. The discussions, negotiations, correspondence and paperwork focus almost exclusively on the interpretation of current regulations applicable to the granting of exemptions from the submission of cost or pricing data. Paperwork, not price, is the issue.

I would like to point out that disclosing proprietary cost data is not, in itself, the only problem. It is the requirement to certify the accuracy of the data based on the Government Cost Accounting Standards. For commercial companies to implement and operate government approved accounting systems for the small amount of dollars that government sales represent would be unreasonably costly, significantly impact our prices, put us at an even greater pricing disadvantage to our foreign competition, and all without providing any benefit to anyone.

Government Inspection and Warranties

Another impediment for commercial vendors doing business with the government is the current requirement for government source inspection. Successful commercial companies have strong commitments to meeting the quality requirements of their commercial customers, both domestic and international. Companies failing to satisfy customers cannot survive in the long run. The quality control process and documentation requirements of the government are largely redundant with our commercial quality control process. More important, we believe that marginal or no added benefit (or improved quality) is achieved as a result of the government inspection process. We have no doubt that the process is justified for firms involved in the manufacture of critical, noncommercial, low volume products and firms with little or no experience in the product field for which they have a contract. Many firms enter businesses only for the contract, not for the long term, and do not have customer feedback driving their quality control processes.

The government seems to start with a presumption that the commercial vendor knows or cares nothing about quality control. In contrast, we believe the government should rely on an established commercial company's quality control system for non-critical commercial products, unless a significant problem arises. Government source inspection should be limited to products involved in mission critical, life or health threatening situations. If a problem does arise, then the commercial vendor could be subject to source inspection until it demonstrates that its quality systems are effective.

The government should also avail itself more of another protection that has proven its effectiveness in the commercial marketplace, i.e. the commercial product warranty. Although one occasionally sees references to the greater use of commercial warranties by the government, from our standpoint, relatively little use of them seems to be occurring.

Although warranty work increases the manufacturer's costs for a particular product, it has several benefits. It provides the manufacturer with critical information about product failures so that improvements can be made. It permits repairs to be made properly and more quickly with the right equipment and trained technicians. It reduces the number of products being returned to the user with improper repairs, thereby reducing customer dissatisfaction with the product. And it provides the commercial vendor with an opportunity to market its maintenance services which often provide a more cost-effective way for customers to maintain their equipment. Tektronix has forty-six sales and service offices throughout the U.S. Our Detroit facility, for example, has some fifty sales and service employees.

Defense Priorities Allocations System

The last impediment I want to talk about today is the improper use of the Defense Priorities and Allocations System (DPAS). As you may know, Section 2071 of Title 50 of the United States Code authorizes the President to require expedited performance under contracts when deemed appropriate to promote the national defense. However, lack of clear regulatory guidance permits virtually unrestricted use of the DPAS rating system. Most of the DOD (and many DOE) orders which we get are DPAS rated.

We recognize the fact that national defense is a high priority. However, unnecessary and unlimited use of the DPAS ratings requires us to develop special and costly order processing procedures, establish special buying requirements, shift productions schedules, and delay delivery to commercial customers. This is particularly troublesome when a priority rating is used in cases where the product is destined for storage in a governme warehouse.

Mr. Chairman, this concludes my remarks. I apologize if they seem negative but I am focusing on the problems. On the positive side, there are many dedicated people in the procurement system who faithfully and conscientiously strive, on a daily basis, to make it work, in spite of the problems with regulations. And I am encouraged that your committee is looking into these problems. We sincerely appreciate your interest in working towards improving the federal acquisition system, especially where commercial product vendors are involved. We believe the issues we have discussed today can be corrected with a little effort on the part of the affected federal agencies if they receive support and direction from policy makers. Removal of these impediments will reduce costs for companies currently doing business with the government, eliminate significant barriers to the entry of new business into the government marketplace, and enable the purchase of commercial products at lower cost to the taxpayer.

I will be pleased to answer any questions you may have.

STATEMENT

OF THE

HONORABLE DONALD ATWOOD

DEPUTY SECRETARY OF DEFENSE

TO THE

UNITED STATES SENATE

* * *

SUBCOMMITTEE ON OVERSIGHT OF GOVERNMENT MANAGEMENT

OF THE

COMMITTEE ON GOVERNMENT AFFAIRS

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DEPARTMENT OF DEFENSE USE OF COMMERCIAL AND NONDEVELOPMENTAL ITEMS

* * *

Washington, D.C.

June 1, 1989

Thank you Mr. Chairman, Distinguished Panel Members, I am pleased to have the opportunity to speak to you about our initiatives to buy and use more commercial products. The DoD has had an ongoing program in this regard since 1976 and some significant improvements have been made. We now use simplified, performance oriented specifications called Commercial Item Descriptions to buy over 3000 clearly commercial products. We have replaced a large number of military specifications and standards with ones prepared by non-Government standards writing organizations such as the Society of Automotive Engineers, the American Society for Testing and Materials, and others. The number of such documents formally adopted for use by DoD is well over 4000. For example, we buy thousands of fasteners, even for critical aerospace applications, to the National Aerospace Standards of the Aerospace Industries Association.

We have worked in a number of areas to simplify contracting for commercial products. The Services and Defense Logistics Agency conducted a complete review of their supplements to the Federal Acquisition Regulation to delete or change unnecessary or overly restrictive regulations. The total line count of the regulations was reduced by approximately 30 percent with no degradation to regulatory guidance. The Department has also completed a study of nearly 500 different regulatory requirements tied to dollar thresholds. The study recommended elimination of almost 20 percent of the thresholds, and modification of another 12 percent.

As a result of a change to the Defense Federal Acquisition Regulation Supplement, which eliminated the need to recompete items on GSA Schedules, we have increased our use of GSA's Multiple Award Schedules by 20 percent over the past two years. Cooperation with GSA on multiple award and other types of Federal Supply Schedules has gotten stronger and more aggressive. The phaseout of mandatory use provisions increases the authority of contracting officers as recommended by the Packard Commission, while allowing direct placement of orders against GSA Schedule contracts in the overwhelming majority of cases where DoD requirements are best met by such action. We have established a program to allow waiver, on a test basis, of FAR, DFAR, and Service Supplemental provisions, that are not required by law. The program has resulted in more than 500 requests for waiver, and has a 60% approval rate.

But while I can describe these and other actions taken to improve our ability to buy commercial products, it would be misleading for me to imply that we are doing all that we can - - or all that we will do to further the goal of making optimum use of commercial and other nondevelopmental items, and to take advantage of the awesome power of innovation and competition which is readily available and waiting for us in the commercial marketplace.

In testimony before this committee two weeks ago you heard several examples of over-specification of requirements. I could defend some of the actions of the Services, but that clearly is not the point. The point is that we are frequently guilty of over-specifying what we need. Anyone with the time and patience to go through our index of nearly 50,000 specifications, standards, and related documents, will be able to find an example. I'm glad to be able to say that, with a little patience one could also find examples of where we have significantly improved on an existing specification, or replaced a Mil Spec with a simpler description of some sort. In the past several years we have worked diligently to reduce the number of different specifications on soldering. There were 135 Military specifications, 84 Service specifications, and 185 industry standards that represented not only dozens of variations in soldering techniques, but several completely different approaches to soldering. This plethora of documents was replaced with a single document - Mil Std 2000. It was a huge step in the right direction, but it was not yet success. In January of this year, a new revision to 2000 was issued, and although the industry is now asking us to hold the target still for a while, the new 2000 represents a move toward acceptance of best commercial practice in soldering. On a simpler scale - Mil Spec fruit cake has made the Washington Post more than once in the past few years. The fourteen page Mil Spec which we used to use has been replaced by a simplified Commercial Item Description occupying only the front and back of a single page. Last year we bought 42 tons of fruitcake at $1.61 per pound.

Specifications and standards form the skeleton around which the defense acquisition process is built. They are necessary to satisfy the primary objectives of procurement - to obtain required products in the proper quantity, of suitable quality, in the time needed, and at the lowest price. The importance of these documents, and standardization in particular, cannot be overemphasized. In his book "Out of the Crisis," Dr. W. Edward Deming acknowledges that standardization was our number one weapon in World War II, and is responsible for providing the American consumer with lower prices, better quality, greater safety, and more productivity.

We still have a number of out-of-date and technologically obsolete documents that significantly contribute to the quality and producibility problems that ultimately inhibit our industrial competitiveness. Industry has identified a few high-usage, cost-driver specifications and standards where removal of obsolete, marginal, and unrealistic requirements could yield substantial savings. While the

Department of Defense has been actively promoting the use of non-Government standards, the Packard Commission noted that substantial savings could be achieved by even greater reliance on these private sector standards for commercial products and processes. Using non-Government standards helps support our industrial base by taking advantage of commercial items and processes already proven in the marketplace, thus enhancing our mobilization capability during a national emergency.

One of the major problems with our specifications and standards is that while the old problems may improve or worsen to some degree, they never seem to disappear. We have looked at our policies to determine if there is some void that needs to be filled, and have concluded that if existing policies were being fully implemented, most of the recurring problems associated with our specifications and standards would not exist. For example, the Department of Defense has an over-age document review policy that requires all specifications and standards that are more than five years old to be reviewed for technical adequacy and to ensure compliance with current policies. After this review, over-age documents are either to be validated as still current for use in acquisition, updated, cancelled, or inactivated for new design. As of November 1987, appropriate action had not been taken on about 5400 over-age documents listed in the index. We also have policies that emphasize performance specifications over "how-to" specifications and non-Government standards over military and federal specifications and standards, and again, there are examples of noncompliance with these policies. What seems to be missing, and what must change if we are to eliminate the recurring problems identified with our specifications and standards, is accountability by the Services and Agencies to demonstrate adherence to the existing policies.

While old problems persist, new ones and new opportunities arise in our rapidly changing world that affect specifications and standards. Our approach to specifications and standards was developed over 35 years ago, and while it is still effective for mature technologies and the reprocurement of commodities intended for repair or replacement, traditional ways of doing business in today's fast-moving, high-tech environment are ineffective. Today, a product can be developed, marketed, and become obsolete in the time it takes to develop a traditional military or private sector specification. For those specifications which will be used in development, we must create highly-flexible documents that allow the insertion of new technologies, new products, and new ideas.

In order to be more responsive to current and future acquisition needs, restore credibility to our existing specifications and standards, eliminate valid criticism of our documentation, and generally revitalize the Defense Standardization Program, there are six broad areas where action must be taken: (1) establish accountability within the Services and Agencies for achieving the program objectives; (2) conduct a comprehensive review of all existing specifications and standards to ensure compliance with Department of Defense policies; (3) establish closer relationships with industry associations and non-Government standards bodies; (4) automate data bases that serve as tools in the development, storage, retrieval, dissemination, application, and analysis of specifications and standards; (5) establish a budget line item controlled by the Office of the Secretary of Defense to aid the Services and Agencies with special standardization projects; and (6) promote greater training for the developers and users of specifications and standards to effect a necessary cultural change. Taking action in these areas will correct persistent problems, ensure these problems do not recur, and will allow us to seize new opportunities to perform our mission more efficiently.

Another issue that you heard about at your first round of hearings was a proliferation of contract clauses that drive commercial suppliers away from doing business with the Department of Defense. We do not dispute that Defense contracts are lengthy, that they contain many clauses that a commercial contractor would not encounter in daily business in the commercial world, or that some of the provisions of Government contracting discourage contractors from wanting to do business with the DoD. As I mentioned earlier, we have taken some steps to simplify our contracting, but some issues remain. Much of what is perceived as contractual complexity is based on statutory requirements, reaction to Comptroller General decisions, or on different end item use requirements. For example, in a study done for the Scientific Apparatus Manufacturers Association, it was found that of 183 clauses specified in the Federal Acquisition Regulation for fixed price contracts, only 97, slightly more than half, had no commercial counterpart. Of those 97, 54 of the clauses directly implement statute. The current statutes seek to maximize competition by ensuring every source that wants to manufacture a product has the opportunity to compete and by favoring awards to sources offering the lowest prices. Operating within those constraints, contracting officials adopt specifications early in the acquisition process in an attempt to ensure suitable products are routinely purchased within tolerable timeframes. To deal with these kinds of issues, we have been working with the Office of Federal Procurement Policy on draft legislation that would provide some relief from statutorily imposed contract clauses and would encourage buying to achieve the best value rather than the lowest initial price.

The commercial-style procedures authorized by the proposed statute would incentivize users to require items that are commercially available and tested in the marketplace, identifying those that are most suited for DoD's needs, and selecting the product constituting the best value. Contracting officials would have an efficient means for integrating their analyses of program needs, commercially available options, and budgetary considerations with the aim of determining the optimal tradeoff. The proposed statute would also relieve contracting officers from the mandatory imposition of a wide variety of statutorily imposed contractual conditions which, as illustrated by several of the witnesses last month, are simply inappropriate for use in contracts for commercial products. Some of these provisions have strong constituencies which can be counted on to oppose any attempt to back away from "across the board" application, irrespective of the inefficiencies and high cost that may be introduced by such rigid adherence to their cause. None-the-less, if we are to significantly improve our ability to buy commercial products, the issues must be addressed.

Another issue raised in the industry testimony was the current requirement for government source inspection and the use of commercial warranties. Industry felt that Government quality assurance requirements add cost without adding quality and are redundant to the contractor's quality control program, at best, or out of date with industry advances in quality control in the worse case. There are currently no regulations which preclude DoD from using warranties for commercial type items. On the contrary, the use of warranties, including contractors' standard commercial warranties, is encouraged. However, warranties are not used as a substitute for quality assurance requirements. The scope of a normal commercial warranty is simply not inclusive enough to ensure quality. They warrant against defects in materials and workmanship; they do not guarantee performance of the item, nor do they guarantee the quality of any item upon production. Warranties also place a number of burdens on the buyer, such as transportation and administration.

I feel a more productive area to pursue is the acceptance of contractor process control and inspection procedures, where they have proven to be satisfactory. The FAR currently limits Government reliance on contractor inspection of commercial items to small purchases. We recently initiated a change to FAR which will eliminate the small purchase limit for commercial and off-the-shelf items. This case is still pending. Once approved, it will allow for contractor inspection of all commercial and off-the-shelf, noncritical items. This should virtually eliminate the additional cost and the inconvenience that are incurred when commercial contractors must make changes to their standard procedures in order to satisfy the Government inspection requirements.

One issue addressed by nearly every witness at the industry hearing was the imposition, and flow down of the requirement for cost or pricing data. I agree with my colleagues form industry that we have gone too far in demanding the submission of such certified data. The DoD has taken several steps to ensure that we do not "over-spec" our requirements in this very sensitive area.

In May of 1987, we issued policy to contracting officers emphasizing that cost or pricing data are not required when adequate price competition is anticipated. The DoD Supplement to the Federal Acquisition Regulation was recently revised to provide additional coverage on adequate price competition. The new coverage explains that adequate price competition may exist even where price is not a primary factor in evaluation of proposals, regardless of the type of contract contemplated. When there is a reasonable expectation that adequate price will result on a particular procurement, the contracting officer should rarely have a need to require the submission or certification of cost or pricing data. Unnecessarily requiring the submission of cost or pricing data is not in the best interest of the Government because it leads to increased proposal preparation costs, extends procurement leadtime, and wastes both contractor and Government resources.

We have also recently drafted a proposed revision to the Federal Acquisition Regulation to clarify and expand on the use of price analysis as a demonstration of adequate price competition when catalog or market prices are claimed by the contractor. Views of interested parties will be sought on the proposed revision. One of our main objectives is to further the policy to buy commercial products by relying on price analysis techniques to the maximum extent possible in negotiations. We have proposed restructuring the designation of sales categories to broaden commercial exemption criteria and give the contracting officer greater latitude for judgement in determining whether the product is sold in substantial quantities to the general public. For example we are proposing that the category of sales to the Government exclude sales based on price competition. Price competition includes sales made from a GSA Multiple Award Schedule contract priced on the basis of an established commercial catalog. We have also proposed an alternate procedure within a specified dollar threshold that excludes highly commercial companies from submitting an SF 1412 "Claim for Exemption from Submission of Certified Cost or Pricing Data," when certain criteria are met. No pre-award audit would be made, if the contractor certifies that the prices offered are not higher than the lowest price charged any customer under similar terms, conditions and quantities. However a post award audit may be performed and a price reduction clause would be included in the contract when the alternate procedure is used. The draft also specifically addresses new and discontinued commercial products that are not based on a catalog or market price and states that the offeror must provide adequate information so that the contracting officer can ensure that any difference in price is identified and justified by use of price analysis. We anticipate that the change will streamline and simplify the current requirement yet still be in compliance with the requirements of the Truth in Negotiations Act.

A measure of the reason that cost or pricing data is so frequently cited as an impediment, is that the ever-present oversight of the General Accounting Office, the Defense Department Inspector General, and the Defense Contract Audit Agency, drive our contracting officers to do what is safest and most easily documented. A contracting officer will seldom ignore the suggestion by any one of these auditing arms, that they should acquire additional data in order to assure a fair and reasonable price. Senator Cohen acknowledged in the previous hearing that Congress may have to accept some of the responsibility for some of the over-regulation. I believe that what Senator Cohen described is exactly the case - that agencies interpret your concern and perhaps become overly zealous in the application of the remedy. I believe that an expression of the sense of Congress, to your audit and investigation arm, that they may be guilty of such excess enthusiasm would be helpful. The over-zealous pursuit of mountains of data to support cost reasonableness is leading to the loss of authority and responsibility of contracting officers, to the loss of commercial vendors from the DoD's competitive base, and to substantial cost to the Government.

I believe that we can not afford to continue to miss opportunities to tap the strength of our commercial industrial base. We can not continue to demand compliance to unrealistic specifications, nor to enforce excessively burdensome and intrusive contract requirements. It is no longer defensible, in these times of constrained budgets, when everyone is trying to do more with less, that we continue to try to duplicate in regulation, the very efficient market forces that keep our commercial industries strong, and fiercely competitive, in the highly charged commercial marketplace.

I am firmly committed to taking DoD beyond rhetoric, paperwork, and good intentions. I sincerely appreciate the interest of this Committee, and pledge to you that, in partnership with you, we will make a difference. We will make acquisition of commercial and other nondevelopmental items the rule, when appropriate, rather than an all too rare exception.

STATEMENT

BY

Greg Saunders

Assistant for Commercial Acquisition

TO THE

UNITED STATES SENATE

* * *

SUBCOMMITTEE ON OVERSIGHT OF GOVERNMENT MANAGEMENT

OF THE

COMMITTEE ON GOVERNMENT AFFAIRS

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DEPARTMENT OF DEFENSE USE OF COMMERCIAL AND NONDEVELOPMENTAL ITEMS

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Washington, D.C.

June 1, 1989

My name is Greg Saunders. I am a staff engineer in the Office of the Deputy Assistant Secretary of Defense for Total Quality Management. I have been, for the past three years, the Department's point man for efforts aimed at buying more commercial products and nondevelopmental items and therefore gave myself the title of Assistant for Commercial Acquisition. I am responsible for initiating actions that would help to move DoD toward greater use of commercial products, for working with the Services, Defense Agencies, and other OSD staff on policy and guidance in that area. I have worked closely with the Services in development of their policies and procedures for acquisition of commercial products, and with the staff of the Deputy Assistant Secretary for Procurement on various procurement policy initiatives including several cases for the Defense Acquisition Regulatory Council. I have participated on two Defense Science Board Task Forces charged with examining and recommending improvements to our capability to buy commercial products. The second of those Task Forces is within a few weeks of issuing a final report, the recommendations of which I expect to be charged with implementing.

The 1986 DSB Task Force observed that they could not address the acquisition of commercial products without examining the underlying buying principles. They said that how you buy in large measure determines what you buy. Mrs Spector has discussed some of the issues surrounding our acquisition process. I would like to comment briefly on how we describe our requirements.

Early in the DoD's history of trying to make greater use of commercial products, the Defense Logistics Agency conducted a test program called the Commercial Commodities Acquisition Program. This test made the first use of the highly simplified purchase descriptions which eventually became known as Commercial Item Descriptions. During the test, a number of clearly commercial products such as t-shirts, gloves, towels, thermometers, x-ray film, and mustard were purchased "off-the-shelf." The test was an unqualified success with purchases of products that not only were adequate, but in many cases were of better quality than those purchased previously to Military Specifications. In 52 buys worth over 40 million 1976 dollars, there was an average of 2.4 additional bidders per solicitation, end item quality was equal or better in all but a very few cases, prices were lower by 10%, deliveries came approximately a month earlier, and awards to small business were up by 1%, not significant as an increase but very significant in showing that small business was not harmed by this process. Following this successful test, the DoD institutionalized preparation of the short, simplified CIDs, and encouraged a fast track program of replacement of Mil Specs with either non-Government, industry prepared and accepted standards, or CIDs. A key to the success of the program was a requirement that in order to be considered, the offeror must be able to show "commercial market acceptability." This was essentially a requirement that said that if you wanted to sell a commercial product to the Department of Defense, you must have a commercial product and be able to demonstrate that you sell that product in the commercial marketplace. The significance of this requirement was that it allowed us to substitute the very efficient test of the commercial marketplace for the detailed quality assurance requirements traditionally written into Military Specifications. It was quite effective and had broad support from commercial vendors who had been trying for years to break into the DoD market, but were not willing to reformulate their products to meet our specifications or to allow our inspectors to infiltrate their facilities.

In order not to simply pull the rug out from under suppliers who had built businesses around supplying DoD Mil-Specs items, we included a "grandfather" provision that allowed Mil-Spec suppliers to continue to offer and be evaluated to the old specification for three years after publication of the CID for their product. In 1983, because such a small business, Government supplier recognized the likelihood of his lock on our business evaporating, he complained to his Congressman and was able to get a provision placed in the DoD Appropriations Act that restricted us from continuing to use commercial market acceptability. This restriction eliminated the basis on which we were able so successfully to buy truly commercial products. It essentially removed "commercial" from our commercial acquisition program. It forced us to go back to use of detailed product descriptions and quality assurance provisions in order to provide some assurance of acquiring suitable products.

In 1986, after much discussion with Congressional staffers, the restriction was removed from our Appropriations Act. Although the specific restriction had been lifted, the Competition In Contracting Act, with it's heightened emphasis on "full and open competition" has kept us from returning to the practice of requiring commercial market acceptability as a condition of bidding. The ability to restrict competition for clearly commercial products to commercial suppliers seems logical and fair, and is necessary if we are to be able to further simplify our specifications and to encourage participation by top quality, commercial suppliers.

In spite of this limitation, we have been able to make some progress in some areas. We have expanded our use of GSA's Multiple Award Schedules and are currently working on a program to include some high dollar value, complex items such as construction and materials handling equipment. As Mr. Atwood told you, we have greatly increased our participation with non-Government standards writers and have adopted more than 4300 such documents for use in acquisition. We have helped to start several non-Government standards committees for commercial items such as food products, food service equipment, and others. With the steps outlined in Mr. Atwood's testimony, we expect to make continued progress in replacing Military documents, eliminating outdated requirements, and accelerating our movement toward stating requirements in terms of performance or functions to be performed instead of with excessive design detail. We will also continue to work toward proper selection of specifications and tailoring of standards and statements of work to try to eliminate such problems as those described by Mr. Rossow where the packaging selected seemed to be completely inappropriate for the product being acquired.

I would like to conclude my statement with a brief discussion of the state of policy and guidance with regard to use of commercial and other nondevelopmental items. The DoD issued it's first Directive on commercial acquisition in 1978. Despite several attempts to update that policy statement, the 1978 Directive is still in effect. The current draft has been in preparation and coordination since just after passage of the NDI preference legislation. Recognizing that the Defense Science Board, as well as this Committee, is likely to give us some new guidance, we have decided to start from a clean sheet of paper, and my marching orders are to make issuance of new, clear, direction a top priority. While an update to that policy is certainly desirable, the Directive that is in place clearly states the necessary policy principles. It states that "DoD Components shall purchase commercial, off-the-shelf, products when such products will adequately serve the Government's requirement..." The DoD Directive on Major System Acquisition, the program managers overriding policy direction states that development shall be undertaken only after carefully assessing use of an existing U.S. or Allied military or commercial system that fosters a non-developmental acquisition strategy, or modification or improvement of an existing system. The policy to our acquisition managers is clear, but while policy is necessary, it is not sufficient to ensure implementation.

Each of the Services has issued guidance manuals to help their acquisition personnel to evaluate and make use of commercial and other nondevelopmental items, and a DoD level manual is in draft. In response to requests for assistance in identifying existing products, we recently issued, a pamphlet describing a number of on-the-shelf, commercially available data bases that help to match requirements with products that are readily available.

We have some success stories. We, unfortunately, have too many stories like those you heard at the earlier hearing. The cultural change necessary to make NDI the automatic first choice, has not occurred. As a strong advocate of using commercial products, I sometimes have to remind myself that acquisition of commercial products is not the goal. The goal is to buy the best product for the job, at the best price. Where that is a commercial or nondevelopmental item, there should be no obstacles to acquiring that product. We will continue to work toward more complete implementation of NDI preference and elimination of barriers to use of commercial products in the DoD.

STATEMENT

OF

MRS. ELEANOR R. SPECTOR

DEPUTY ASSISTANT SECRETARY

OF DEFENSE (PROCUREMENT)

BEFORE THE

SUBCOMMITTEE ON OVERSIGHT OF

GOVERNMENT MANAGEMENT

COMMITTEE ON GOVERNMENTAL AFFAIRS

JUNE 1, 1989

MY NAME IS ELEANOR SPECTOR AND I AM THE DEPUTY ASSISTANT SECRETARY OF DEFENSE FOR PROCUREMENT. I AM RESPONSIBLE FOR ESTABLISHING THE PROCUREMENT POLICIES OF THE DEPARTMENT, INCLUDING THOSE POLICIES WHICH AFFECT THE ACQUISITION OF COMMERCIAL PRODUCTS. HOWEVER, I AM NOT RESPONSIBLE - NOR ARE MOST CONTRACTING PERSONNEL - FOR DETERMINING WHAT WE NEED TO BUY OR HOW THESE REQUIREMENTS WILL BE DEFINED IN SPECIFICATIONS OR STATEMENTS OF WORK. THIS SEEMS TO ME TO BE THE ROOT OF THE PROBLEMS IN DOD'S ACQUISITION OF COMMERCIAL PRODUCTS.

I AM NOT SUGGESTING THAT CHANGES TO OUR PROCUREMENT POLICIES ARE NOT NECESSARY TO ENCOURAGE THE ACQUISITION OF COMMERCIAL PRODUCTS. WE ARE NOW CONSIDERING CHANGES TO THE FEDERAL ACQUISITION REGULATION WHICH WOULD:

- FURTHER THE POLICY TO BUY COMMERCIAL PRODUCTS BY RELYING ON PRICE ANALYSIS TECHNIQUES TO THE MAXIMUM EXTENT POSSIBLE IN NEGOTIATIONS.

- o RESTRUCTURE THE DESIGNATION OF SALES CATEGORIES TO BROADEN COMMERCIAL EXEMPTION CRITERIA AND GIVE THE CONTRACTING OFFICER GREATER LATITUDE FOR JUDGMENT IN DETERMINING WHETHER THE PRODUCT IS SOLD IN SUBSTANTIAL QUANTITIES TO THE GENERAL PUBLIC.

- o EXCLUDE PREDOMINANTLY COMMERCIAL COMPANIES FROM SUBMITTING AN SF 1412 "CLAIM FOR EXEMPTION FROM SUBMISSION OF CERTIFIED COST OR PRICING DATA" WHEN CERTAIN CRITERIA ARE MET

THESE ARE MATTERS WHICH HAVE BEEN OF GREAT CONCERN TO COMMERCIAL SUPPLIERS. WE EXPECT THAT OUR PROPOSED CHANGES WILL BE REVIEWED BY THE DAR COUNCIL IN JUNE AND WILL BE A SIGNIFICANT STEP IN REMOVING IMPEDIMENTS TO THE PURCHASE OF COMMERCIAL PRODUCTS.

MANY OF THE IMPEDIMENTS TO THE ACQUISITION OF COMMERCIAL PRODUCTS ARE NOT IMPOSED BY DOD. ON MAY 16, MR. PINICK OF BOEING TESTIFIED BEFORE THIS COMMITTEE THAT NINETEEN FEDERAL ACQUISITION REGULATION CLAUSES REQUIRING FLOW DOWN TO BOEING'S VENDORS INHIBITED THE SALE OF

A MODIFIED 757 AIRCRAFT TO THE US NAVY. ALL NINETEEN OF THESE CLAUSES ARE REQUIRED BY STATUTE. EACH SESSION OF CONGRESS SEES MORE LEGISLATION IMPOSED ON DOD WHICH MAKES US A LESS DESIRABLE CUSTOMER TO COMMERCIAL CONTRACTORS. WILL CONTRACTORS BE MORE OR LESS LIKELY TO SEEK OUT DOD CONTRACTS AS A RESULT OF THE CERTIFICATION REQUIREMENTS OF THE "PROCUREMENT INTEGRITY" PROVISIONS OF THE OFPP REAUTHORIZATION ACT? ANOTHER EXAMPLE OF LEGISLATION WHICH WILL DISCOURAGE COMMERCIAL CONTRACTORS IS THE LIQUIDATED DAMAGES PROVISIONS OF THE SMALL BUSINESS OPPORTUNITY DEVELOPMENT REFORM ACT (P.L. 100-656). WHEN CONTRACTORS FAIL TO MAKE A GOOD FAITH EFFORT TO MEET SMALL BUSINESS SUBCONTRACTING GOALS THEY MUST PAY LIQUIDATED DAMAGES . THIS EVEN APPLIES TO GSA'S MULTIPLE AWARD SCHEDULE CONTRACTS. THIS FURTHER DEPRESSES INTEREST IN GOVERNMENT CONTRACTS AMONG COMMERCIAL SUPPLIERS.

THE COMPETITIVE PROCEDURES CURRENTLY REQUIRED BY LAW WERE NOT DESIGNED WITH COMMERCIAL PRODUCTS ACQUISITION IN MIND. THE CURRENT STATUTES SEEK TO MAXIMIZE COMPETITIONS BY ENSURING EVERY SOURCE THAT

WANTS TO MANUFACTURE A PRODUCT HAS THE OPPORTUNITY TO COMPETE INCLUDING SMALL AND SMALL DISADVANTAGED BUSINESSES EVEN WHEN THEY DO NOT HAVE SUBSTANTIAL SALES TO THE PUBLIC. OPERATING WITHIN THOSE CONSTRAINTS, CONTRACTING OFFICIALS FIND THAT DETAILED SPECIFICATIONS MUST BE ADOPTED EARLY IN THE ACQUISITION PROCESS TO ENSURE THAT SUITABLE PRODUCTS ARE ROUTINELY PURCHASED WITHIN TOLERABLE TIMEFRAMES. FURTHER, UNDER THE MINIMUM NEEDS DOCTRINE, SOMETIMES REVISING REQUIREMENTS TO TAKE ACCOUNT OF KNOWLEDGE GAINED THROUGH MARKET RESEARCH IS CONSIDERED TO IMPLY BIAS.

TO HELP CORRECT SOME OF THESE DEFICIENCIES, WE HAVE BEEN WORKING WITH THE OFFICE OF FEDERAL PROCUREMENT POLICY TO DEVELOP A LAW WHICH WOULD ENCOURAGE REQUIREMENTS PEOPLE TO SPECIFY COMMERCIAL ITEMS BECAUSE BUYING THEM WOULD BE QUICKER THAN A MILITARY SPECIFICATION ITEM. ALLOWING THE COMMERCIAL MARKET PLACE TO SUBSTITUTE FOR THE VERY COMPLEX PROCUREMENT SYSTEM NOW REQUIRED WOULD SAVE TIME AND MONEY.

THE PURPOSE OF THE BILL IS TO REQUIRE THE DEVELOPMENT OF COMMERCIAL-STYLE PURCHASING

PROCEDURES TO BETTER UTILIZE MARKET RESEARCH, AVOID OVER-SPECIFICATION, AND OTHERWISE FACILITATE THE ACQUISITION OF COMMERCIAL PRODUCTS. THE DRAFT BILL HAS MANY DESIRABLE FEATURES:

(1) IT PROVIDES A PROCEDURE FOR PURCHASING COMMERCIAL ITEMS THAT APPROXIMATES COMMERCIAL-STYLE ACQUISITION.

(2) IT PROVIDES VARIATIONS TO THOSE PROCEDURES WHICH MAY BE USEFUL IN PROCURING SOME COMMERCIAL-TYPE ITEMS.

(3) IT PROVIDES GREATER AUTHORITY TO THE CONTRACTING OFFICER IN ESTABLISHING TIME PERIODS FOR SYNOPSIS AND RECEIPT OF OFFERS.

(4) IT ALLOWS FOR AWARDS BASED ON BEST VALUE.

(5) IT ALLOWS FOR AWARD WITHOUT DISCUSSIONS.

PROCUREMENTS WOULD BE INITIATED WITH A PUBLIC NOTICE REQUESTING INTERESTED SOURCES TO MAKE SUBMISSIONS DESCRIBING THEIR PRODUCTS AND EXPLAINING HOW THEY MEET THE ADVERTISED

NEEDS. THE PUBLIC NOTICE WOULD BE ISSUED AS SOON AS CONTRACTING OFFICIALS WERE ABLE TO EXPLAIN NEEDS IN CONCEPTUAL TERMS. COMMERCIAL PRODUCTS WOULD BE REQUIRED TO HAVE ACHIEVED MARKET ACCEPTANCE AND TO COMPLY WITH MINIMUM, FUNDAMENTAL REQUIREMENTS SYNOPSIZED IN THE PUBLIC NOTICE. THESE COULD INCLUDE COMMERCIAL STANDARDS, MINIMUM FUNCTION AND PERFORMANCE LEVELS, ESSENTIAL FORM AND FIT SPECIFICATIONS, AND IN APPROPRIATE CASES, DOD MANUFACTURING PROCESS QUALIFICATION STANDARDS.

CONGRESS ITSELF MUST BE A PART OF THE SOLUTION IN THE ACQUISITION OF COMMERCIAL PRODUCTS.

was received unless such amounts are authorized to be appropriated after the date on which such report was received.".

(2) The table of sections at the beginning of such chapter is amended by adding after the item relating to section 2436 (as inserted by section 905) the following new item:

"2437. Defense enterprise programs: milestone authorization.".

(b) Initial Designation of Participating Programs.—The Secretary of Defense shall designate for fiscal year 1988 not less than three defense enterprise programs to be considered for milestone authorization under subsection (b). The Secretary shall make such designations as part of the budget submission of the Department of Defense for such fiscal year.

SEC. 907. PREFERENCE FOR NONDEVELOPMENTAL ITEMS

(a) In General.—(1) Chapter 137 of title 10, United States Code, is amended by adding at the end the following new section:

"§2325. Preference for nondevelopmental items

"(a) Preference.—The Secretary of Defense shall ensure that, to the maximum extent practicable—

"(1) requirements of the Department of Defense with respect to a procurement of supplies are stated in terms of—

"(A) functions to be performed;

"(B) performance required; or

"(C) essential physical characteristics;

"(2) such requirements are defined so that nondevelopmental items may be procured to fulfill such requirements; and

"(3) such requirements are fulfilled through the procurement of nondevelopmental items.

"(b) Implementation.—The Secretary of Defense shall carry out this section through the Under Secretary of Defense for Acquisition, who shall have responsibility for its effective implementation.

"(c) Regulations.—The Secretary of Defense shall prescribe regulations to carry out this section.

"(d) Definition.—In this section, the term 'nondevelopmental item' means—

"(1) any item of supply that is available in the commercial marketplace;

"(2) any previously-developed item of supply that is in use by a department or agency of the United States, a State or local government, or a foreign government with which the United States has a mutual defense cooperation agreement;

"(3) any item of supply described in paragraph (1) or (2) that requires only minor modification in order to meet the requirements of the procuring agency; or

"(4) any item of supply that is currently being produced that does not meet the requirements of paragraph (1), (2), or (3) solely because the item—

"(A) is not yet in use; or

"(B) is not yet available in the commercial marketplace.".

(2) The table of sections at the beginning of such chapter is amended by adding at the end the following new item:

"2325. Preference for nondevelopmental items.".

(3) The Secretary of Defense shall prescribe regulations as required by section 2325(c) of title 10, United States Code (as added by subsection (a)(1)), before the end of the 180-day period beginning on the date of the enactment of this Act.

(b) Removal of Impediments to Acquisition of Nondevelopmental Items.—(1) The Secretary of Defense shall submit to the Committees on Armed Services of the Senate and House of Representatives a report—

(A) identifying actions taken, including training of personnel and changes in regulations and procurement procedures, to implement the requirements of section 2325 of title 10, United States Code (as added by subsection (a)(1));

(B) identifying all statutes and regulations that are determined by the Secretary to impede the acquisition of nondevelopmental items by the Department of Defense; and

(C) recommending any legislation that the Secretary considers necessary or appropriate to promote maximum procurement of nondevelopmental items to fulfill the supply requirements of the Department of Defense.

(2) The Secretary shall take appropriate steps to remove any impediments identified by the Secretary under paragraph (1)(A) that are under the jurisdiction of the Secretary.

(3) The report required by paragraph (1) shall be submitted before the end of the one-year period beginning on the date of the enactment of this Act.

(c) Evaluation by Comptroller General.—(1) The Comptroller General shall conduct an independent evaluation of the actions taken by the Secretary of Defense to carry out the requirements of section 2325 of title 10, United States Code (as added by subsection (a)(1)).

(2) The Comptroller General shall submit to the Committees on Armed Services of the Senate and House of Representatives a report on the evaluation required by paragraph (1). Such report shall include—

(A) an analysis of the effectiveness of the actions taken by the Secretary to carry out the requirements of section 2325 of title 10, United States Code (as added by subsection (a)(1));

(B) a description of any programs conducted to notify acquisition personnel of the Department of Defense of the requirements of such section and to train such personnel in the appropriate procedures for carrying out such section;

(C) a description of each law, regulation, and procedure which prevents or restricts maximum practicable use of nondevelopmental items to fulfill the supply requirements of the Department of Defense; and

(D) such recommendations for additional legislation as the Comptroller General considers necessary or appropriate to promote maximum procurement of nondevelopmental items to fulfill the supply requirements of the Department of Defense.

(3) The report required by paragraph (2) shall be submitted before the end of the two-year period beginning on the date of the enactment of this Act.

(d) Definition.—For the purposes of subsections (b) and (c), the term "nondevelopmental items" has the meaning given such term in

section 2325(d) of title 10, United States Code (as added by subsection (a)(1)).

SEC. 908. REQUIREMENTS RELATING TO UNDEFINITIZED CONTRACTUAL ACTIONS

(a) LIMITATION ON USE OF FUNDS FOR UNDEFINITIZED CONTRACTUAL ACTIONS.—(1) On the last day of each six-month period described in paragraph (4), the Secretary of Defense (with respect to the Defense Logistics Agency) and the Secretary of each military department shall determine—

(A) the total amount of funds obligated for contractual actions during the six-month period;

(B) the total amount of funds obligated during the six-month period for undefinitized contractual actions; and

(C) the total amount of funds obligated during the six-month period for undefinitized contractual actions that are not definitized on or before the last day of such period.

(2) On the last day of each six-month period described in paragraph (4), the amount of funds obligated for undefinitized contractual actions entered into by the Secretary of Defense (with respect to the Defense Logistics Agency) or the Secretary of a military department during the six-month period that are not definitized on or before such day may not exceed 10 percent of the amount of funds obligated for all contractual actions entered into by the Secretary during the six-month period.

(3) If on the last day of a six-month period described in paragraph (4) the total amount of funds obligated for undefinitized contractual actions under the jurisdiction of a Secretary that were entered into during the six-month period exceeds the limit established in paragraph (2), the Secretary—

(A) shall, not later than the end of the 45-day period beginning on the first day following the six-month period, submit to the defense committees an unclassified report concerning—

(i) the amount of funds obligated for contractual actions under the jurisdiction of the Secretary that were entered into during the six-month period with respect to which the report is submitted; and

(ii) the amount of such funds obligated for undefinitized contractual actions; and

(B) except with respect to the six-month period described in paragraph (4)(A), may not enter into any additional undefinitized contractual actions until the date on which the Secretary certifies to Congress that such limit is not exceeded by the cumulative amount of funds obligated for undefinitized contractual actions under the jurisdiction of the Secretary that are not definitized on or before such date and were entered into—

(i) during the six-month period for which such limit was exceeded; or

(ii) after the end of such six-month period.

(4) This subsection applies to the following six-month periods:

(A) The period beginning on October 1, 1986, and ending on March 31, 1987.

(B) The period beginning on April 1, 1987, and ending on September 30, 1987.

THE UNDER SECRETARY OF DEFENSE
WASHINGTON, DC 20301

ACQUISITION

28 JUL 1987

(P&L/PS)

MEMORANDUM FOR COMMANDANT, DEFENSE SYSTEMS MANAGEMENT COLLEGE

SUBJECT: Commercial and Nondevelopmental Item Acquisition

As you know, the Department of Defense is placing increased emphasis on the acquisition of commercial-off-the-shelf and other nondevelopmental items (NDI) where they will meet our needs. A large part of the success of our efforts will hinge on program managers and their staffs making the right decisions and planning for the use of NDI early in their programs. We need to assure that commercial and NDI acquisitions are thoroughly covered in your Program Managers and Executive Refresher courses. Additionally, in order to reach appropriate field personnel, we need to consider developing a series of workshops to be given at your regional offices. Additional background material is attached.

Your support on this issue is crucial if we are to be successful. My action officer, Mr. Greg Saunders, 695-7915, is available to work with your staff at your earliest convenience.

Attachment

ISSUE PAPER

ISSUE:

Educate program managers and staffs regarding benefits of using nondevelopmental items (NDI), the logistics implications of NDI decisions, and in specifications of requirements to avoid premature foreclosure of NDI solutions.

PROPOSED ACTION:

Develop a module for inclusion in the 19-week Program Managers Course (PMC). Ensure that NDI is adequately treated throughout the PMC. Include a segment in the three-week executive refresher course. Conduct a series of workshops at regional offices, possibly working with other Service schools such as AFIT, to cover more detailed discussion of cost/performance trade-offs, logistics considerations, and specification techniques.

BACKGROUND:

Both the Packard Commission and the Defense Science Board recognized the benefits of greater use of commercial products and buying practices. Both recommended that DoD take appropriate steps to increase use of commercial products. The FY 1987 Authorization Act also charges DoD with, among other things, reporting on actions taken to train program managers in the acquisition and use of NDI. A three tiered approach is recommended in order to get needed training to program managers who are already in place and working as well as to those PMs we are developing through the PMC. The first tier would be a module of training to be included in the PMC, and the inclusion of NDI considerations in other appropriate modules of the PMC curriculum. The second tier would be a module to be included in the PM Executive Refresher course. The third, and perhaps most important tier, would be a series of workshops to be conducted at DSMC regional training centers. The workshops would include some case studies and some more detailed discussion of cost/performance tradeoffs, logistics support, standardization, and spares availability considerations, specification techniques which would provide for NDI solutions, and any special contracting techniques that may encourage use of commercial or other nondevelopmental items. The workshops could be equally beneficial to item managers and to base commanders trying to implement model installation techniques.

POINT OF CONTACT:

The action officer in OSD is Mr. Greg Saunders, 695-7915.

DEPARTMENT OF DEFENSE
DEFENSE SYSTEMS MANAGEMENT COLLEGE
OFFICE OF THE COMMANDANT
FORT BELVOIR, VIRGINIA 22060 5426

DSMC-PMCPO September 3, 1987

MEMORANDUM FOR: The Under Secretary of Defense for Acquisition, The Pentagon, Room 3E808, Washington, D.C. 20301

SUBJECT: Commercial and Non-developmental Item Acquisition

1. In your memorandum of 28 July 1987, you indicated that you wanted increased emphasis on the Non-Developmental Item (NDI) acquisition strategy in the College courses. The College has begun a concentrated effort to include more on the NDI strategy.

2. NDI, as an element of a program's acquisition strategy, is addressed in two of the three DSMC Executive courses within discussions of current initiatives in acquisition management policy. Knowledgeable speakers from OSD and the Services have been used to share their understanding and experience with the course participants. In the third executive course, the Executive Management Course, discussions of NDI implementation is incorporated into a 4-hour workshop session addressing formulation and execution of acquisition strategies and plans. Additionally, in a 4-hour workshop on program risk assessment, the impact of a NDI strategy is investigated.

3. In the Program Management Course, NDI is also addressed as an alternative to new system development. The participants are challenged to develop an NDI acquisition strategy considering both the advantages and challenges in implementing such a strategy. Specifically, the engineering and logistic implications are explored and workable strategies are developed. This same block of instruction is also presented in the 1-week course, Fundamentals of Systems Acquisition Management. This course is offered at the Fort Belvoir campus as well as in the regions. The College is also developing a 3-hour PMC elective to provide further guidance on implementing a NDI strategy.

4. The College has also begun research into alternative procurement approaches of which NDI is a major area of concentration. To help with this research, the theme of the Technical Management Advanced Workshop, a 1-week course, will be the implications of alternative procurement approaches. We are asking the Services to nominate three of their senior managers to attend this workshop. From this effort, it may be feasible to develop a workshop which may be given in the regions as well as at Fort Belvoir.

Charles P Cabell Jr

CHARLES P. CABELL, JR.
Brigadier General, USAF
Commandant

AGU0251637

DoD Report to the Armed Services Committees of the Senate and the House of Representatives on Nondevelopemental Item Acquisition, Progress and Impediments

~~December 1987~~

Introduction

In 1972, the Commission on Government Procurement issued a report recognized as being the earliest formal call for government to buy more commercial products rather than relying on uniquely designed products to meet materiel requirements. In the fifteen years since that report was issued, the Department of Defense (DoD) has done many things to increase reliance on commercial products:

- Issued policy and implementation guidance in DoD directives, manuals, and letters,
- issued implementing changes to acquisition regulations (ASPR, DAR, FAR, and DFARS), and to other directives governing procurement,
- conducted seminars, symposia, and conferences, to acquaint acquisition personnel with advantages, risks, and special considerations involved in use of commercial products,
- issued Service and Agency Regulations manuals, and policy letters establishing programs for increased use of commercial products,
- developed modules for inclusion in courses training specification writers, program managers, and contracting personnel,
- established a new series of product descriptions called "Commercial Item Descriptions" (CIDs),
- modified military specifications to eliminate noncommercial requirements except where absolutely necessary,

- significantly increased use of non-government standards,
- established the Foreign Weapons Evaluation Program.

Each of these actions contributed to increasing use of commercial and other nondevelopmental items, (NDI) where they meet the users needs. There are numerous examples of commercial products being used today where military unique products were the norm only a few years ago. Examples range from obvious commercial products such as T-shirts, catsup, and office equipment, to more complex items such as trucks, materials handling equipment, navigation radios, complicated electronic test equipment, and medical equipment such as C/T scanners and x-ray devices. Major systems such as the Air Force's KC-10 tanker aircraft, the Army's Logistics Support Vessel, and the Navy's P-3 Orion replacement submarine hunter aircraft are, or will be based on modifications of nondevelopmental items. In publications that cover military acquisition, the phrase "off-the-shelf" appears with increasing frequency when referring to acquisition planning for major and less-than-major systems. Complex and detailed military specificatons for items such as fruit cakes, worcestershire sauce, laboratory flasks, batteries, and a host of other readily available commercial items have been replaced by simplified CIDs which state, in a few pages, the salient characteristics of the product that is needed. Use of draft requests for proposals (RFPs) seeking industry comment and proposal of NDI solutions to operational requirements has increased steadily over the past several years.

But even with the clear accomplishments and progress that has been made, acquisition of commercial off-the-shelf, NDI, and modified commercial and NDI systems, equipment, and supplies, is the exception rather than the rule. The President's Blue Ribbon Commission on Defense Management recommended that even greater emphasis be placed on meeting DoD needs with commercial products, and that there be changes in regulations to promote use of commercial buying practices. The Congress responded by including a section titled "Preference for Nondevelopmental Items" in the Defense Acquisition Improvement Act of 1986. The section requires that DoD state its needs in terms of performance required, functions to be performed, and essential physical characteristics, and mandates that nondevelopmental items be acquired to meet those needs to the maximum extent practicable. It further requires the Secretary of Defense (SecDef) to report to the Armed Services Committees of the Senate and the House of Representatives identifying actions taken to implement that section, and identifying those laws and regulations that impede the acquisition of nondevelopmental items, and to take action to abate through regulations those impediments which are in his power to change, or by submission of proposed legislation those that would require new or revised statutes.

Although statutes and regulations can be identified as disincentives to greater acquisition of commercial and other NDIs, they are not prohibitive. If elimination of a few provisions of law or regulation was the answer to increasing use of commercial products and buying practices, the changes would have been proposed long ago. Increasing the acquisition of commercial products has been the subject of numerous studies by various prestigious organizations including the Defense Science Board, the Georgetown Center for Strategic Analysis, the Analytical Sciences Corporation, the law firm of Hogan and Hartson, and the Commercial Product Acquisition Team, to name a few. None of the studies have identified a simple solution for achieving the objective.

This report identifies actions DoD has taken, identifies impediments, disincentives, and areas where there is a lack of incentive, and discusses areas where further work is either underway or planned.

Actions Taken

In the past two years a number specific actions have been taken to encourage, train, and enable DoD personnel to buy and use more commercial and other nondevelopmental items.

- The Defense Science Board conducted a study on use of commercial components in military equipment. The study report, issued in January 1987, made numerous recommendations for improving the Department's ability to buy and use commercial products. The Military Departments and DoD Agencies are cooperating with the Office of the Secretary (OSD) to implement the recommendations.

- The Defense Systems Management College, the principal training center for DoD program managers, has begun offering modules in each of their courses, on NDI acquisition. The courses cover benefits techniques, risks, and special considerations such as logistics support, inherent in such acquisition. The courses also cover cost-performance tradeoffs to obtain best value for DoD.

- A DFARS section was implemented in April 1987, requiring market analyses and early consideration of nondevelopmental items to meet acquisition needs.

- A full-time position was established on the OSD staff responsible for taking appropriate actions to encourage use of NDI and advocating policy and procedural changes to enhance ability to buy NDI.

- The DoD Directive and Instruction (DoDD 5000.1 and DoDI 5000.2), which are the primary regulations governing system acquisitions, were revised in September 1987 to require priority consideration of the use of nondevelopmental items as is or with modifications, to satisfy materiel requirements.

- A revision to DoD Directive 5000.37 on Acquisition and Distribution of Commercial Products stresses the broader implications of use of nondevelopmental items. It provides direction and guidance on appropriate testing, logistics support, standardization considerations, and other areas requiring spocial consideration in NDI acquisitions. The directive is in coordination and is expected to be issued early in 1988. The revision authorizes publication of a manual to provide detailed guidance and techniques for NDI acquisition. A first draft of the manual has been prepared and publication is expected soon after issuance of the directive.

- A study is being conducted by the Logistics Management Institute to identify exisiting data bases which provide information on commercial products. The study will result in a pamphlet for distribution in early 1988 to program and item managers to assist them in performing market analyses of available products.

- Contracting officers were reminded by a May 1, 1987 memorandum that cost or pricing data should not be obtained when adequate price competition is anticipated.

- Thresholds for field pricing reports and audits have been increased to $500,000 for fixed-price contracts and $1,000,000 for cost reimbursement contracts.

Impediments

The Defense Acquisition Improvement Act of 1986, Public Law 99-500, section 907(b) requires DoD to identify "all statutes and regulations that are determined by the SecDef to impede the acquisition of nondevelopmental items by the DoD..." To comply with this requirement, the Department solicited the views of private industry by means of an August 17 notice in the Federal Register. Responses from that solicitation, along with input from other sources such as the Commercial Product Acquisition Team and from reports, studies, and discussions with DoD contracting and program management personnel were used to compile this report. Some of the items listed implement significant public policy and their impact on the efficiency of DoD acquisition may be less important than the greater national objectives that they seek to accomplish.

The following is a listing and brief discussion of specific impediments that were identified. Some issues seem relatively minor when considered individually but the cumulative affect of numerous such issues can be significant. Additionally, many of the issues that were identified are not unique to commercial or NDI acquisition but affect a broad range of government procurement and are being addressed through various acquisition improvement initiatives. Actions are underway to alleviate many of the impediments and others are being further reviewed for appropriate action.

1. Procurement activities have separate record keeping systems for such items as Small and Disadvantaged Business Subcontracting Plans. There is little or no sharing of information among buying organizations, forcing contractors to submit such plans each time they do business with a different contracting activity.

2. The government sometimes demands warranties that are beyond those normally offered on commercial products. Warranties on

goods sold to the government should be the same as warranties to industry unless the government has specific reason to require more and is willing to pay for the additional protection.

3. Although DoD is not responsible for administration of the GSA multiple award schedule program, as a user it is concerned about the program. There are some rules for participation in the GSA schedule program which discourage qualified offerors from participating. These rules include:

- A requirement for most favored customer pricing when the government is not necessarily a favored customer.
- A price reductions clause which requires extensive record keeping.
- Maximum order limitations that do not reflect quantity price break-points.
- Government access to records and data.

4. Costly and time consuming testing is frequently required of all offerors prior to award. Policy should require testing of only apparent winner.

5. Minor modifications of commercial products tend to result in very small and inefficient production runs. The modifications can also activate certain government intrusion into the commercial manufacturers facilities for product and plant inspections. Modifications to commercial products also activate provisions which require major changes in commercially-adequate accounting systems and record keeping. These include:

- cost or pricing data in accordance with Public Law 87-653
- allowable costs certification

- cost accounting standards in accordance with Public Law 91-379

- application of cost principles

6. Marking of packing cases with local stock numbers and unique government bar coding rather than relying on the Universal Production Code costs additional money and disrupts normal commercial packing and marking operations.

7. There are situations where cost or pricing data are required even though prices appear to be set by market conditions or by competition, because the particular circumstances do not precisely meet the exemption criteria provided under the law. Situations where cost or pricing data requirements may not be justified except for the requirement of law included:

- Although specific guidance has recently been issued (May 1,1987) that contracting officers should not request cost or pricing data when adequate price competition is anticipated, such data is sometimes still requested as insurance against criticism.

- Sales of product to the private sector originally met percentage requirements to be exempt from submission. Large government buys skew the percentage to the extent that subsequent buys no longer qualify for the exemption even though the product is still being sold in the same substantial quantities to the general public.

- A newly developed product, clearly intended for sale to the general public, but without a history of "substantial sales" to the general public.

- Percentages of sales to the general public applied restrictively to specific model numbers. Most times this is reasonable, but when the government buys spares for systems that it is maintaining beyond the normal commercial life, it may be buying a part that is the same as or similar to one with a different part number used in a more recent system. The new part cannot be substituted, and the older part is no longer sold to the commercial world.

- Even though the catalog or market price exemption applies to services, it is seldom used for anything but the most mundane of services. The government is therefore incapable of obtaining, for example, engineering services for which there are market and catalog prices on other than a cost basis. When contractors must set up separate cost centers for their government business, there is a demonstrably higher cost.

8. Inappropriate use of government specifications and standards levies requirements on commercial products to operate in environments to which they will never be subjected. Additionally, Mil Spec components are sometimes required in system design to achieve a certain level of reliability and environmental resistance. In some instances, appropriate setting of end product performance parameters would allow for use of proven commercial products instead of more costly products designed around the Mil Spec components.

9. NDI acquisitions, where some additional capability is required to meet DoD needs, require offereors to incur development, testing, tooling, and facilitization costs in order to be responsive to solicitation requirements. This shifts development costs from the government to all of the offerors, frequently resulting in decreased competition where offerors are unwilling or unable to subsidize these costs. When conducted correctly, NDI acquisition should result in selection of an existing item which, by evaluation or testing, demonstrates the best potential to meet the user's requirement with a minimum of development, cost, schedule, or technical risk.

10. Government requirements for rights in technical data differ significantly from normal practice in the private sector. Requirements for reprocurement packages, spare part support, maintenance, and training drive government buyers to seek unlimited data rights. Contractors are forced to choose between not bidding and risking release of technical data essential to their competitive position in the commercial marketplace.

11. Government contracts for commercial products include the same clauses used in developmental contracts. While they may be appropriate for large cost reimbursable contracts, the cumulative effect of such clauses is to create a considerable impediment for commercial vendors wishing to do business with the government. Such clauses which seem inappropriate for commercial contracting include:

- Required source identification--requiring identification of the sources of supply for items to the government.

- Conflicts of interest in defense contracting--requiring annual reporting concerning compensation to certain former DoD employees.

- Validation of proprietary data restrictions--allowing contracting officers to demand written justification for any restriction asserted by the vendor on the right of the U. S. to use technical data provided under a contract.

- Commercial pricing for spare or repair parts (10 USC 232)--requiring the collection and certification of data on the pricing of certain items.

- Employee fraud, waste, and abuse awareness programs--requiring commercial vendors to establish an employee orientation program for the prevention of fraud, waste, and abuse in government contracts.

- **Truth in Negotiations Act--lowering the threshold for submittal of cost or pricing data from $500,000 to $100,000.**

12. Inappropriate and inconsistent contract clauses used by different government agencies, different Departments and Agencies within the DoD, and different buying organizations within a Department or Agency cause confusion and uncertainty and increase a contractor's risk in doing business with the government.

13. The period for which offers for sale of commercial goods to the government must remain valid substantially exceeds that of the commercial marketplace. The commercial norm of 30 days is routinely doubled, and is sometimes extended to 90 to 120 days adding cost and exposure to liability for comercial vendors accustomed to the shorter acceptance period.

14. The requirement that product upgrades which do not affect form, fit, or function be documented with a contract modification results in delivery delays and added cost to the contractor. Even when a contractor wants to pass a price reduction on to the government, a contract modification must be processed.

15. Quality assurance program, inspection, traceability, inspection record keeping, and governmental surveillance requirements are inconsistent with modern commercial QA procedures. The repetitive nature of compliance with these requirements and sign-offs by DoD personnel add unnecessary costs without increasing protection or benefits for the government.

16. The lack of any ability for contracting organizations to effectively limit competition to only proven commercial suppliers leads to use of excessively detailed product

descriptions in order to assure requisite quality, and to the necessity of evaluating sometimes hundreds of offers.

17. The current protest system which provides for easy access to protest by disgruntled offerors and the cataclysmic consequences of protests leads contracting officers to do the things that are the most easily documented and supported rather than things which may result in the best buy for the government.

18. The provision in the 1983-1985 Defense Authorization Acts limiting DoD's use of commercial market acceptability as a prequalification to bidding has been removed. The DFARS case implementing the Conference Report condition to protect small business "contract manufacturers" has encountered difficulties. Commercial market acceptability was successfully used to ensure usability, especially of common commercial products such as food products and common hardware items. It had an adverse impact, however, on "contract manufacturers" who make products only for government. A DFAR case was prepared to allow for submission of product samples from apparent winners who could not demonstrate commercial market acceptability. After considerable study, however, it was determined that the proposed procedures subvert the bidding process. The DAR council is examining alternatives, but a solution has yet to be found.

Future Actions

Considerable work continues to be done to improve the DoD's ability to buy and use commercial and other nondevelopmental items. This section of the report discusses areas that are in work, planned, or are under consideration. These items address many of the impediments that have been identified, but also address areas where program managers, contracting officers, and prime and subcontractors can be incentivized to buy and use more NDI.

1. DoD is working with the Office of Federal Procurement Policy on proposed legislation for commercial products. Although the final form of the propsal has yet to be determined, the overall concept is to recognize commercial acquisition as something different from the normal way of doing business. Such acquisition would be subject to a set of terms and conditions that more nearly reflects contracting in the commercial world. A standard, uniorm commercial contract reflecting these terms and conditions could be developed and used as the basis for all "commercial contracting." Under this concept, "commercial contracting" would be exempt from certain laws and regulations governing other forms of government contracting, and implementation of certain other laws and regulations would be modified to reduce government's intrusion in the management and control of private industry by simplifying, reducing, or eliminating some certifications, reporting, and record keeping requirements. Areas to be considered under this concept would include:

- Redefinition of when cost or pricing data would be required including treatment of sales to the government based on established catalog prices or adequate price competition as "sales to the general public" to eliminate the built-in penalty for doing business with the government.

- Reestablishment of the Contractor Weighted Average Share for determining reasonableness of indirect costs, where cost or pricing data is necessary.

- Establishment of a simplified disallowance factor for unallowable costs based on a certification from vendor accounting firms that indirect costs are allocated in conformity with generally accepted accounting principles.

- Establishment of a methodology for qualification of suppliers.

- Exemption, for competitive procurement of commercial and other nondevelopmental items, from certain laws including:

  - Required source identification
  - Conflicts of Interest in Defense Procurement
  - Employee Fraud, Waste, and Abuse Awareness Progams
  - Walsh-Healy
  - Davis-Bacon
  - Service Contracts
  - Buy American
  - Use of American Flag Carriers
  - Protests
  - Etc.

- Establishment of simplified dispute resolution procedures.

2. Coverage in DFARS on acquisition planning has been modified to include serious consideration of acquiring commerical or nondevelopmental items. Consideration is being given to expanding and strengthening the coverage to include requirements for early and thorough market research and analysis and, above some dollar threshold (e.g., for procurements expected to be over $500,000) a requirement for early public notice to industry of functional requirements stated in broad terms, inviting comment and proposals of NDI and modified commercial or NDIs to

meet the requirements.

3. DoD use of Federal Multiple Award Schedules (MAS) is being emphasized. Consideration should be given to establishing DoD MAS for items which have limited or no demand by other Federal Agencies. As a user of MAS, DoD will work with GSA to improve and simplify the schedule system. Areas suggested for possible improvement include:

- Clarifying negotiating objectives.
- Modifying maximum order limitations to maximize price break points.
- Changing time-of-delivery requirements.
- Making contract modification procedures less slow and cumbersome .
- Modifying reporting requirements.
- Examining policies for government access to records and requirements for additional data.
- Simplifying the administration of provisions for price increases and economic price adjustments.
- Clarifying contract language with respect to commitments, warranties, and representations.

4. FAR and DFARS sections on use of specifications, standards, and other purchase descriptions are being revised to indicate a clear preference for product descriptions which will result in procurement of commercial or other nondevelopmental items.

5. Consideration is being given to prividing expanded FAR and DFAR sections on acquisition of commercial products with

explicit regulatory guidance for government contract personnel. Specific areas of concern include:

- The definition of commercial products.
- Guidance on the conduct and importance of market research and analysis.
- Guidance on acceptability to include such factors as availability, life-cycle costs, product improvements, training programs, prior product history, prior test information, prior experience, availability of product support programs, warranties, and potential suitability of a product with modifications.
- Guidance on acquiring "best value" rather than lowest initial cost.

6. DoD Directives and Instructions have been and are being revised to provide positive direction encouraging acquisition of commercial and NDI rather than simply being permissive.

Summary

Much of what has to be done to increase acquisition and use of commercial and other nondevelopmental items involves changing attitudes as well as regulations. The DoD has an aggressive program to modify policies and procedures, and to propose legislation where appropriate, to alleviate impediments and to create incentives to buy and use nondevelopmental items. Perhaps as important as these concrete actions is the clear, strong support of top level executives and officers in the Services, Defense Agencies, and OSD.

We believe that significant progress is being made as is evidenced by the number of NDI products and systems being acquired or seriously evaluated to satisfy materiel requirements. We also recognize that there are numerous areas for continued improvements and will maintain a high level of emphasis on exploiting these opportunities.

DoD Report to the Armed Services Committees of the Senate and the House of Representatives on Nondevelopmental Item Acquisition, Progress and Impediments

December 1987

Introduction

The nondevelopmental item (NDI) approach of encouraging the use of existing items as an alternative to developing new items to meet military needs has been used for many years by the Department of Defense (DoD). In recent years, NDI has received greater emphasis because of the growing recognition that it can save money and time, reduce system obsolescence, and provide proven items.

In 1987, the Army, Navy, Air Force, and Defense Agencies continued their extensive use of the NDI approach. The following are a few recent examples:

- The Army Communications and Electronics Command has 75 NDI programs, including a $4.6 billion award to the international team of GTE/Thomson-CSF for an Army battlefield telephone system that is based on the French RITA mobile subscriber system, and $1 billion to buy NDI computer hardware and software for the Army Command and Control System.
- The Army Research, Development, and Engineering Center awarded a $15.6 million contract to Phrobis III, Ltd. to buy more than 300,000 bayonets that were derived from the commercially available Buck-Master hunting knife.
- The Naval Air Engineering Center saved $13.9 million by using previously developed electro-optic support equipment instead of the planned development of new F/A-18 Forward Looking Infrared Support Equipment.
- The Navy is evaluating an NDI approach to buy 125 patrol aircraft to replace the aging P-3 Orions. Some industry NDI proposals include modernization of the existing Lockheed P-3, the McDonnell Douglas MD-87, and a modified Boeing 757.

- On June 30, 1987, the Army christened the first of four NDI logistic support vessels which will support unit redeployments and resupply missions in remote, undeveloped areas along coastline and inland waterways.
- Air Force policy directs use of NDI in all Communications-Computer Systems Architecture acquisitions except for unique mission equipment embedded in major weapons systems developments. A family of requirements contracts has been developed to implement this policy. Current acquisitions, administered by Air Force Communications Command, include a standard microcomputer contract to Zenith Corporation; a standard minicomputer contract to satisfy larger organizational/ functional data processing requirements which is nearing award, a standard Local Area Network (LAN) components contract, and a group of contracts to provide Base Information Digital Distribution System (BIDDS) components Air Force-wide.

These are recent examples of nondevelopmental items being bought by the military, where special military items were the norm only a few years ago. Notwithstanding these accomplishments and the progress that has been made, the DoD acknowledges that more NDI opportunities exist.

Recognizing the need to place greater emphasis on fulfilling DoD needs with nondevelopmental items, the Congress included a section 907 titled "Preference for Nondevelopmental Items" in the Defense Acquisition Improvement Act of 1986. This legislation provided a statutory preference for NDI acquisition, and required the DoD to state its needs in terms of performance required, functions to be performed, and essential physical characteristics, and it mandated that NDI be used to the maximum extent practicable. The legislation also required the Secretary of Defense to report to the Armed Services Committees of the Senate and House of Representatives on: (1) the actions taken by the DoD to implement the NDI legislation; (2) any statutory or regulatory impediments to NDI acquisition; and (3) any recommended legislation to promote maximum use of NDI acquisition. This report responds to this legislative requirement.

Actions Taken to Implement NDI Legislation

Since the enactment of the "Preference for Nondevelopmental Item" legislation, the DoD has taken the following actions to change regulations and acquisition policies, to train personnel, and to generally promote greater use of NDI acquisition.

- The DoD Federal Acquisition Regulation Supplement was revised in April 1987 to require the DoD to fulfill its needs through the acquisition of nondevelopmental items to the maximum practicable extent.

- The primary regulations (DoD Directive 5000.1 and DoD Instruction 5000.2) governing both major and non-major defense system acquisitions were revised in September 1987 to require consideration of NDI alternatives before starting new development programs. The Mission-Need Statement must describe any known alternatives to new development that will be considered, and the System Concept Paper and Decision Coordinating Paper must discuss why an NDI system was not selected.

- The DoD Directive on commercial acquisition (DoDD 5000.37) is being changed and expanded to promote NDI acquisition. The proposed revision to the directive is in coordination and will be issued in 1988.

- The proposed revision to DoDD 5000.37 authorizes publication of an NDI Manual to provide detailed guidance and techniques for NDI acquisition. The manual is being developed, and will be issued by the end of 1988.

- The Logistics Management Institute will publish a study in early 1988 to identify existing data bases which provide information on commercial products. This study will produce a pamphlet to assist program and item managers in performing market analyses of available products.

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- An OSD chaired steering group with high-level members from the Services and DLA was established in May 1987 to address ways to implement the recommendations of the President's Blue Ribbon Commission on Defense Management and the 1986 Defense Science Board Summer Study on the Use of Commercial Components in Military Equipment.

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- The Defense Systems Management College, the principal training center for DoD program managers, has begun offering modules on NDI acquisition in each of their courses. The modules cover benefits, techniques, risks, and special considerations, such as logistics support, inherent in such acquisition.

- A full-time position was established on the OSD staff in December 1986 to encourage use of NDI and advocate policy and procedural changes to increase NDI acquisition.

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Impediments

In order to identify impediments to NDI acquisition, the DoD solicited the views of private industry by means of a notice in the Federal Register. In addition, reports and studies from a private industry group known as the Commercial Product Acquisition Team (COMPACT) and other sources, and discussions with DoD contracting and program management personnel were used to identify impediments. The COMPACT report was particularly detailed, and the DoD is evaluating the COMPACT observations. A preliminary evaluation of the report indicates many of the concerns raised are addressed below.

An analysis of the input has not revealed any specific regulation or statute that could be construed as a major barrier to NDI acquisition. Rather, the impediments can generally be characterized as hinderances which can discourage commercial vendors from seeking DoD business.

The following impediments have been evaluated, and corrective action, if required, has been identified.

- Impediment #1 - Contracts for nondevelopmental items include unnecessary clauses and there are too many and too complex regulations.

  Comments/Action Taken - To remedy this impediment, the DoD has taken steps to modify the acquisition system to rely more on individual authority and accountability and use commercial-style procurement methods. These actions support the Presidential Task Force on Regulatory Relief. Legislative reform proposals to streamline and improve the acquisition process are being developed. Regulations and field procedures are being reviewed to identify rules that are not required by law or are unnecessarily restrictive. Ideas are being collected from field personnel, various acquisition studies, and industry. The Military Departments are working to

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reduce the number, volume, and complexity of their acquisition regulations. Innovative procurement methods are being tested through the Pilot Contracting Activities Program for possible application throughout the DoD. These actions should make it easier for field commanders and managers to get the quality products and services they need, when they need them, and at a reasonable price.

- Impediment #2 - Cost Accounting Standards (CAS) are an impediment to getting commercial companies into the defense business. CAS is a requirement of law on certain defense contracts and subcontracts. Commercial businesses believe that complying with CAS is not worth the effort for a small amount of defense business.

Comments/Actions Taken - The requirements of CAS are stringent and may require a commercial business to make changes in their accounting systems. However, CAS is only a requirement of law for negotiated defense contracts. Any items provided by commercial businesses under sealed bids in a competitive environment are not required to include CAS provisions. In addition, any contract or subcontract with a small business is excluded from CAS coverage. Therefore, it is possible for many commercial businesses to obtain defense contracts without worrying about complying with CAS. Even if a commercial business negotiates contracts for defense business, CAS may not be applicable. For example, all contracts under $100,000 are excluded as well as any contract under $500,000 if the business does not already have a CAS covered contract. A commercial business could have a number of defense contracts under $500,000 and still not meet the CAS requirements until the total of the awards exceeded $10 million in a given year or the total awards represented more than 10 percent of the firm's business. Also, contracts for truly commercial, "off-the-shelf" items which have a catalog or market price based on substantial sales to the general public do not have a CAS requirement. If a commercial company has a truly unique product which is required by the DoD, it is also possible to obtain a waiver from CAS from the Deputy Assistant Secretary of Defense for Procurement under procedures outlined in Part 30 of the Federal Acquisition Regulation. There are strict requirements which must be met to obtain a waiver, but waivers have been granted in the past, and are a distinct possibility depending on the type of product or service. ∴ CAS is not an impediment.

- Impediment #3 - Government requirements for rights in technical data differ significantly from normal practice in the private sector. Requirements for reprocurement packages, spare part support, maintenance, and training drive government buyers to seek unlimited data rights. Contractors are forced to choose between not bidding and risking release of technical data essential to their competitive position in the commercial marketplace.

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Comments/Action Taken - Contractors do not release technical data in commercial practice. Since technical data is not patented, nondisclosure protects market position. However, the DoD requires technical data to operate, maintain, and overhaul the systems it acquires which are frequently on the leading edge of technology and frequently used in remote or hostile environments. To enable the government to obtain technical data that is the proprietary property of a contractor, the contractor may limit government's right to use proprietary technical data to internal government purposes thereby protecting the contractor's market position. However, this precludes use of the technical data for competitive procurement. In order to compete contracts for future requirements, certain buying activities were requiring contractors to sell or relinquish to the government the right to disclose their proprietary technical data outside the government in order to receive a contract award. As a result, contractors were forced to choose between not bidding and risking release of proprietary technical data essential to their competitive position in the commercial marketplace. Action was taken to correct this through the issuance of new technical data regulations in May 1987. The new regulations balance the government's need to encourage innovation and private development with the need to obtain rights in technical data for the purpose of competition. Contractors' rights in technical data resulting from their own privately funded development efforts are protected. The regulations direct Contracting Officers to obtain only the minimum data and data rights essential to meet needs and further directs that they may not require contractors to sell or relinquish their proprietary rights in technical data. Decisions to obtain data must be fully justified with consideration given to such factors as whether the data pertains to "commercial items." Data pertaining to "commercial items" is to be obtained only when clearly justified as necessary. The regulations also attempt to further encourage innovative technological development at private expense by permitting contractors to retain sole access to the commercial market where the development effort is funded by both the government and the contractor. In the past, any government contribution to the development effort resulted in the government receiving the right to use and release the data outside the government without restrictions on further use. We believe that these changes to our policy will make privately funded development more attractive to government contractors and remove their concerns about selling commercial items to the government.

- Impediment #4 - There are some rules for participation in the GSA multiple award schedule program which discourage qualified offerors from participating.

- A requirement for most favored customer pricing when the government is not necessarily a favored customer.
- A price reduction clause which requires extensive record keeping.
- Maximum order limitations that do not reflect quantity price break-points.
- Government access to records and data.

Comments - GSA has responsibility for the federal supply schedules and is therefore responsible for the rules and regulations pertaining to the schedules. While some companies may consider the GSA regulations to be an impediment, preliminary discussions with GSA personnel indicate that most companies are bidding and participating in the federal supply schedule process. Unless more significant type problems develop with regard to use of the schedules, the DoD does not consider this to be a major impediment.

- Impediment #5 - The Truth-In-Negotiations Act serves as an impediment, in some cases, to NDI acquisition.

Comment/Actions Taken - Cost or pricing data are required to be submitted only on noncompetitive, negotiated contracts of more than $100,000. Contracts awarded on the basis of adequate price competition, or where the contracting officer determines that the price offered is based on catalog or market prices of commercial items sold in substantial quantities to the general public, are exempt from the requirements of the Act. Where catalog or commercial items require some modification peculiar to the needs of the government, cost or pricing data need not be obtained if the cost of such modification is not more than $100,000. The DoD alleviated some of the problems by raising the threshold for requiring audit reports from $100,000 to $500,000 on fixed-price contracts and from $500,000 to $1,000,000 for cost type contracts. A DoD policy memorandum was issued in May 1987 to emphasize that cost or pricing data are not required when adequate price competition is anticipated. The policy memorandum included guidance to contracting officers describing the circumstances constituting adequate price competition.

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Recommended Legislation to Promote NDI Acquisition

The Office of Management and Budget (OMB) will be submitting a bill to Congress titled the "Commercial Products Acquisition Act." The DoD has provided input to the Act and supports its intent to establish streamlined, commercial style, competitive procedures for the acquisition of commercial products, and to eliminate any statutory impediments to the adoption of such procedures. This Act will authorize the use of short form contracts; allow for market acceptability to be a condition for contract award; require evaluation of offers to be based on best value rather than solely on price; and reduce the number of statutes and regulations that apply to commercial acquisition.

Summary

Much of what has to be done to increase acquisition and use of commercial and other nondevelopmental items involves changing attitudes as well as regulations. The DoD has already modified or is in the process of modifying its policies and procedures to alleviate impediments and encourage the acquisition of nondevelopmental items. Perhaps as important as these concrete actions is the clear, strong support of top level executives in the Services, Defense Agencies, and OSD.

We believe that significant progress is being made as is evidenced by the number of NDI products and systems being acquired or seriously evaluated to satisfy materiel requirements. We also recognize that there are areas for continued improvements and will maintain a high level of emphasis on exploiting these opportunities.

THE OFFICE OF THE ASSISTANT SECRETARY OF DEFENSE
WASHINGTON, D.C. 20301-8000

PRODUCTION AND
LOGISTICS
(PS/SDM)

28 DEC 1987

Honorable Sam Nunn
Chairman
Committee on Armed Services
United States Senate
Washington, DC 20510-6050

Dear Mr. Chairman:

The enclosed report provides information regarding efforts by the Department of Defense to implement the legislation on nondevelopmental items (NDI), identify impediments to NDI acquisition, and recommend any necessary legislation to promote NDI acquisition. The report is submitted in response to the requirement in section 907 of the Defense Acquisition Improvement Act of 1987.

We feel that we have made considerable progress improving our ability to buy and use NDI. There are many areas, however, where attention still needs to be focused. The Department will continue to pursue an aggressive program to make greater use of NDI where it meets our needs.

Sincerely,

ROBERT C. McCORMACK
Deputy Assistant Secretary
(Production Support)

Enclosure

THE UNDER SECRETARY OF DEFENSE
WASHINGTON, DC 20301

ACQUISITION

21 APR 1989

Honorable Carl Levin
Chairman
Subcommittee on Oversight of
Government Management
Committee on Government Affairs
United States Senate
Washington, DC 20510-6250

Dear ~~Mr. Chairman~~ Carl:

This is in response to your letter requesting information on the Department of Defense implementation of section 907 of the National Defense Authorization Act for FY 1987 which establishes a preference for nondevelopmental items (NDI). The Department has a good record in moving toward greater use of NDI, and I am pleased to provide you with the enclosed description of actions we have taken. Although we are moving in the right direction, the cultural change necessary to make use of NDI the norm, rather than an exception has not yet occurred. We are continuing to work toward that goal, and to that end, I reconvened the Defense Science Board Task Force on "Use of Commercial Components in Military Equipment." Its report, with specific recommendations, will be out within the next 60 days.

Sincerely,

Enclosures

Status of Current Efforts to Implement Section 907 of the Defense Authorization Act for 1987 Preference for Nondevelopmental Items

(Answers are keyed to the numbered questions in Senator Levin's Letter of March 23)

1. Current status for each bulleted item in the 1987 report under the heading "Actions Taken To Implement NDI Legislation" is as follows:

   - The Department of Defense (DoD) Federal Acquisition Regulation Supplement was revised in April 1987 to require the DoD to fulfill its needs through the acquisition of nondevelopmental items to the maximum practicable extent.

     Current Status: A copy of the changed sections is at attachment 1.

   - The primary regulations (DoDD 5000.1 and DoDI 5000.2) governing both major and nonmajor defense systems acquisitions were revised in September 1987 to require consideration of NDI alternatives before starting new development programs.

     Current Status: A copy of each of the regulations is at attachment 2. Paragraphs D.5 and D.9.f in DoDD 5000.1 and paragraph 6 of enclosure 4 on "System Concept Paper (SCP) and Decision Coordinating Paper (DCP) Formats" to DoDI 5000.2 specifically address NDI acquisition.

   - The DoD Directive on commercial acquisition (DoDD 5000.37) is being changed and expanded to promote NDI acquisition.

     Current Status: The directive has been revised to include coverage of issues such as logistics support, testing and evaluation, areas needing special emphasis, and to expand coverage from only commercial products to include the full spectrum of nondevelopmental items. The directive is being coordinated with the Services, Defense Agencies, and appropriate offices in the Office of the Secretary of Defense.

   - The proposed revision to DoDD 5000.37 authorizes publication of an NDI manual to provide detailed guidance and techniques for NDI acquisition.

Current Status: A draft of the manual has been prepared. It is intended to provide greater detail to program and contracting personnel regarding requirements setting, specification, market research, and contracting techniques.

- The Logistics Management Institute will publish a study to identify existing data bases which provide information on commercial products.

  Current Status: The study was completed and the resulting pamphlet (copy at attachment 3) has been distributed to over 5,000 specification writers, program management, and item management personnel.

- An OSD chaired steering group with high-level members from the Services and DLA was established to address ways to implement the recommendations of both the Packard Commission and the Defense Science Board Summer Study on Commercial Components.

  Current Status: The formality of a steering group that met on a regular basis was deemed unnecessary. However, the points of contact established by creation of the steering group were used to provide high level input on various NDI issues.

- The Defense Systems Management College, the principal training center for DoD program managers, has begun offering modules on NDI acquisition in each of their courses.

  Current Status: While the segment of instruction specifically dedicated to NDI is limited in scope and duration, as was pointed out in the GAO report of February 1989, consideration of NDI alternatives is an integral part of the case study which runs throughout the program managers course. Additionally, several other training courses now include segments on NDI acquisition.

- A full-time position was established on the OSD staff in December 1986 to encourage use of NDI and advocate policy and procedural changes to increase NDI acquisition.

  The position was created and is currently filled.

2. Additional actions that have been taken to implement section 907 since 1987 are described in the report to Congress on "Simplification and Streamlining of Acquisition Procedures" and the report to the Secretary of Defense on "Enhancing Defense Standardization" (copies

at attachments 4 & 5). Specific areas that impact the DoD's ability to buy NDI include, from the Simplification and Streamlining of Acquisition Procedures report:

- the Pilot Contracting Activities Program;
- the Bank Card Program;
- Output from the DoD Contract Simplification Workshop;
- Clarification of when to obtain cost or pricing data;

and from the Enhancing Defense Standardization report:

- the review of specifications and standards;
- Suspension of issuance or revision of Military Specifications in 400 (of 657) Federal Supply Classes;
- Increased reliance on non-government standards.

3. For each impediment identified in the 1987 report, actions taken to remove the impediment are as follows:

Impediment #1 - Contracts for nondevelopmental items include unnecessary clauses and there are too many and too complex regulations.

Actions since 1987 - The Services and Defense Logistics Agency completed a complete review of their supplements to the Federal Acquisition Regulation to delete or change unnecessary or overly restrictive regulations. The total line count of the regulations was reduced by approximately 30 percent with no degradation to regulatory guidance.

The Department has also completed a study of nearly 500 different regulatory requirements tied to dollar thresholds. The study recommended elimination of almost 20 percent of the thresholds, and modification of another 12 percent. The Defense Acquisition Regulatory Council (DARC) is reviewing the recommendations for appropriate action.

The DoD also supports a service sponsored Contract Simplification Workshop aimed at simplifying procedural requirements, reducing redundancies, and eliminating layering of authority and approval levels. Output from the workshop is proposed to the DARC for making permanent changes to acquisition regulations. One significant proposal from a recent workshop deals with a new solicitation cover sheet, a simplified contract format, and the use of annual representations and certifications. The proposed change would permit use of the simplified contract format for firm-fixed price and fixed-price with economic price adjustment acquisitions of noncomplex supplies or services. The case is currently under review.

Impediment #2 - Cost Accounting Standards (CAS) are an impediment to getting commercial companies into the defense business.

Actions since 1987 - Public Law 100-679, the Office of Federal Procurement Policy (OFPP) Act Amendments of 1988, reestablishes the Cost Accounting Standards Board, as an independent board within OFPP. The act provides that the board shall have exclusive authority to make, promulgate, amend, and rescind cost accounting standards and interpretations thereof. The act did, however, raise the threshold from $100,000 to $500,000 for application of the standards to negotiated contracts. This change should be relatively significant in reducing the impediments to the purchase of nondevelopmental items. In addition, as stated in the report to Congress, there are a number of other exemptions to CAS. These have not been changed as the result of reestablishing the CAS board.

Impediment #3 - Government requirements for rights in technical data differ significantly from normal practice in the private sector.

Actions since 1987 - The DoD recognizes the detrimental impact that requiring contractors to sell or otherwise relinquish their legitimate proprietary rights in technical data as a condition for the award of a contract can have on privately funded development and DoD's access to commercial technologies. Not only are such requirements not in the best interest of the Department but they are contrary to existing law. These facts are recognized in DoD's Supplement to the Federal Acquisition Regulation Part 227.4 which expressly prohibits such activities by DoD acquisition personnel. This section of the regulation was extensively revised via DAC 88-2 (December 1, 1988) and DAC 88-3 (December 15, 1988). The latter regulation complies with 10 U.S.C. 2305(d)(4), which was amended under section 806, Incentives for Innovation, of the FY 1989 DoD Authorization Act, Public Law 100-456, on September 29, 1988. The statute limits the the Government's authority to require that prospective developers or producers of major systems provide proposals which would enable the Government to use technical data to obtain future competition when acquiring items or components of the weapon system, where the items or components were developed exclusively at private expense.

Impediment #4 - There are some rules for participation in the GSA multiple award schedule program which discourage qualified offerors from participating.

Actions since 1987 - GSA/DoD cooperation on multiple award and other types of Federal Supply Schedules (FSS) has gotten stronger and more aggressive. It is estimated that DoD's use of GSA/FSS items has increased 10-20 percent in the last two years. This increase resulted from DoD's 1987 change to the Defense Federal Acquisition Regulation Supplement (DFARS 8.404-2(a)(70)) which eliminated the need to recompete items on GSA Schedules which are optional for use by DoD.

Converting GSA Schedules from mandatory to optional use for the Military Departments and Defense Agencies was an additional incentive. Since optional schedules are now considered "preferred sources of supplies and services" within DoD, the phaseout of mandatory use provisions increases the authority of contracting officers as recommended by the Packard Commission while allowing direct placement of orders against GSA Schedule contracts in the overwhelming majority of cases where DoD requirements are best met by such action. As stated in the 1987 report, the Department does not consider GSA schedules as impediments to commercial product acquisitions but rather as quick efficient methods of obtaining needed requirements and indeed a key tool to increase use of commercial products that meet DoD requirements.

Impediment #5 - The Truth-In-Negotiations Act serves as an impediment, in some cases, to NDI acquisition.

Actions since 1987 - In addition to the actions identified in the report to the Congress, DASD(P) has recently drafted a proposed revision to the regulations which apply to established catalog or market prices of commercial items sold in substantial quantities to the general public. The proposed change will streamline and simplify current requirements for determining when to request cost or pricing data, yet still be in compliance with the Truth in Negotiations Act. The draft is currently being reviewed by a small number of government and industry representatives. After evaluating comments received from that group, a case will be submitted to the DARC for consideration.

4. Additional impediments to NDI acquisition have not been specifically identified since issuance of the report in December 1987. Instead, DoD efforts have been directed toward removing or ameliorating the impact of previously identified impediments, and toward development of plans for improving our ability to buy NDI and to use commercial buying practices where it makes sense to do so. As indicated in answer to the previous question, a number of steps have been taken with regard to identified impediments. In addition, the Defense Science Board reactivated its task force on use of commercial components in military equipment and their report, including specific recommendations to implement commercial acquisition in DoD, will be issued within the next 60 days.

5. The DoD/OFPP proposed legislation is in coordination with the other Executive Departments and responses are due by April 25, according to OFPP. Previous editions of the proposal have been endorsed by the DoD, but submittal of a final, approved proposal is the responsibility of Office of Management and Budget.

SUBCOMMITTEE ON OVERSIGHT OF GOVERNMENT MANAGEMENT STAFF ANALYSIS OF DOD'S RESPONSE TO THE SUBCOMMITTEE'S INQUIRY ABOUT ACTIONS TO PROMOTE THE ACQUISITION OF NONDEVELOPMENTAL ITEMS

June 1, 1989

The following is a point-by-point analysis of DOD's response to the Subcommittee's March 23, 1989 letter requesting a status report on actions taken to promote the acquisition of nondevelopmental items (NDI's). The numbered and lettered points in DOD's letter appear in quotation marks, followed by the comments of the Subcommittee staff.

DOD Letter:

"1. Status of bulleted items in the 1987 DoD report to Congress under the heading 'Actions Taken to Implement NDI Legislation.'

"a. The Department of Defense (DoD) Federal Acquisition Regulation Supplement was revised in April 1987 to require the DoD to fulfill its needs through the acquisition of nondevelopmental items to the maximum practicable extent. Excerpts of Part 207.105 (Contents of Written Acquisition Plans) and 210 (Specifications, Standards and Other Purchase Descriptions) are attached."

Subcommittee Staff Comments:

(1) Part 207.105 of the Defense Supplement to FAR Part 7 (Written Acquisition Plans) contains the following subparagraph:

> (b)(6) Product Descriptions. For developmental acquisition, describe the market research efforts planned or undertaken to identify nondevelopmental items (See 210.001) that could satisfy the acquisition objectives.

This is the only place in the Defense Supplement to FAR Part 7 where NDI is mentioned.

This amount of guidance is inadequate in that it fails to require that written acquisition plans include steps to assure that (i) subsystems and components of developmental systems that are NDI candidates are identified, and (ii) contractors ensure that subcontractors use NDIs whenever it is practicable to do so. It should be noted that this section of the FAR and Defense Supplement pertains only to acquisitions of large systems and items of equipment.

(2) The Department of Defense provided an outdated excerpt of DFARS Part 210 (Specifications, Standards, and Other Purchase Descriptions) in its April 21, 1989 letter to the Subcommittee. The current version of this section, as revised in November 1988, was provided to the Subcommittee at the June 1, 1989 hearing. The revised section contains the following new language:

"While there may be some mandatory design or performance requirements applied to a single phase or through the acquisition cycle, the citation of specifications, standards, and related documents shall (i) specify results desired, rather than how to design or how to manage."

The language in the revised version of the Defense Supplement to FAR Part 210 (including the above quotation) addresses the specification issue in a positive manner. However it does not directly implement the statutory language which requires agencies to state their requirements for supplies "to the maximum extent practicable" in terms of "(A) functions to be performed; (B) performance required; or (C) essential physical characteristics." In other words agencies should use product descriptions which describe form, fit, and function. It is not clear why DoD chose not to incorporate this statutory requirement directly into the regulation.

The FAR itself contains provisions that are inconsistent with the statutory preference for NDIs. Paragraph 10.006 of FAR Part 10 (Using Specifications and Standards) mandates the use of specifications and standards listed in the Index of Federal Specifications and Standards. The acquisition of commercial products is treated as a permissible exception to this general rule:

> (b) Commercial Exception. (1) . . . [A]gencies should consider stating their needs in a purchase description, when appropriate under Part 11 and implementing agency regulations, even though there is an indexed specification. (2) The agency responsible for a specification may designate it as one for which this exception cannot be used, if the agency head or a designated representative determines this to be necessary.

In other words, agencies should consider using purchase descriptions (which facilitate the procurement of NDIs) in lieu of military specifications on an exception basis, rather that a preferred basis, as required by the statute.

The DoD supplement does not address this section of the FAR (Paragraph 10.006); therefore, these FAR provisions presumably apply to DoD.

In conclusion, the FAR Part 10 (Specifications, Standards and Other Purchase Descriptions) does not contain language that properly implements the statute with respect to how agencies state their requirements for items of supply. The Defense Department has not remedied this problem as fully as it could have by simply incorporating the statutory language in the DoD FAR Supplement. Without such a clear directive in the regulations, contracting officers may continue to rely on detailed design specifications to describe product needs. Consequently, many contractors that may be capable of fulfilling the government's needs with their off-the-shelf products will simply not compete for the government's business

(3) The DoD response also fails to mention FAR Part 11 (Acquisition and Distribution of Commercial Products) and the Defense Supplement to this part. The language in this part of the FAR predates the enactment of the statutory preference for NDIs. This is the section of the FAR where the statutory preference for NDIs should logically be defined and implemented. This section is inadequate for the following reasons:

(a) The coverage addresses commercial products, rather than nondevelopmental items. Commercial products are a subset of nondevelopmental items; the use of the two terms interchangeably has been the cause of confusion.

(b) The regulatory coverage does not adequately address market research and analysis and product acceptability (e.g., availability, life-cycle costs, modification requirements, prior product history, availability of product support programs, warranties, etc.).

(c) The DoD supplement to this part contains the following provision:

> Contracting activities may use purchase descriptions which allow offerors to furnish commercial products and allow the government to use commercial distribution systems whenever these products or distribution systems satisfy the government's needs, but only if not prohibited by 211.005(b) below.

The prohibition referred to is as follows:

> Solicitations may not exclude small business concerns from being considered for award, whether or not

former suppliers under detailed specifications, solely because the product of the small business does not meet the definition of a commercial or commercial-type product in FAR 11.001.

Stated differently, the government may not exclude a small business concern from competing for contract award simply because the small business cannot prove that its product is sold or traded to the general public in the course of normal business operations at prices based on established catalog or market prices. The prohibition first appeared in the 1983 DoD Supplementary Appropriations Act. It was also enacted in the 1984 DoD Appropriations Act.

This prohibition was deleted from subsequent appropriations acts due to an agreement reached with the House Appropriations Committee that DoD would issue revised guidelines on the acquisition and distribution of commercial products. These revised guidelines have never been issued. Even though the prohibition is no longer required in law, it is still contained in the DoD FAR supplement and is still the DoD policy.

In conclusion, the DoD Supplement does not remedy any of the problems with the basic FAR coverage. The entire FAR Part 211 and the DoD Supplement need to be rewritten and structured in such a manner that all aspects of the statutory preference for NDI are covered.

DOD Letter:

"b. The primary regulations (DoDD 5000.1 and DoDI 5000.2) governing both major and nonmajor defense systems acquisitions were revised in September 1987 to require consideration of NDI alternatives before starting new development programs. Copies of the regulations are attached."

Subcommittee Staff Comments:

Although these revisions are helpful, the regulations referred to are high-level publications that are referred to when new development programs are under consideration. They are not commonly used by the majority of the acquisition community in day-to-day operations.

DOD Letter:

"c. The DoD directive on commercial acquisition (DoDD 5000.37) is being changed and expanded to promote NDI acquisition. Under current status, the directive has been revised to include coverage of issues such as logistics support, testing and evaluation, areas needing special emphasis, and to expand coverage from only commercial products to include the full spectrum of NDI. The directive is being coordinated with the services, defense agencies and appropriate offices in OSD."

Subcommittee Staff Comments:

DoD Directive 5000.37 (Acquisition and Logistical Support of Nondevelopmental Items) has been under review since March 1987. We understand that this regulation has not been published because insufficient resources have been dedicated to its completion.

DOD Letter:

"d. The proposed revision to DoDD 5000.37 authorizes publication of an NDI manual to provide detailed guidance and techniques for NDI acquisition. Under current status, a draft of the manual has been prepared. It is intended to provide greater detail to program and contracting personnel regarding requirements setting, specification, market research and contracting techniques."

Subcommittee Staff Comments:

As with the basic regulation, the NDI manual has been under review since about March 1987. The reason for the delay is lack of sufficient resources dedicated to its completion. The lack of top level emphasis within DoD has resulted in a failure to establish deadlines either for the regulation (DoDD 5000.37) or the manual. The absence of deadlines has resulted in no action being taken.

DOD Letter:

"e. The Logistics Management Institute will publish a study to identify existing data bases which provide information on commercial products. Under current status, the study was completed and the resulting pamphlet has been distributed to over 5,000 specification writers, program management, and item management personnel."

Subcommittee Staff Comments:

The pamphlet was published in February 1989. The pamphlet lists two categories of commercial data bases: federal supply catalog based (which contain both commercial and military products) and commercial product catalog based. It does not list DoD owned and operated data bases, which contain comprehensive information on off-the-shelf products that is useful to government acquisition personnel and is different from the information contained in the commercial data bases.

DOD Letter:

"f. An OSD chaired steering group with high-level members from the services and DLA was established to address ways to implement the recommendations of both the Packard Commission and the Defense Science Board Summer Study on Commercial Components. Under current status, DoD stated that the formality of a steering group that met on a regular basis was deemed unnecessary. However, the points of contact established by creation of the steering group were used to provide high level input on various NDI issues."

Subcommittee Staff Comments:

This group, which was established in May, 1987, took no substantive action and was disbanded. This is a good example of the low priority that DoD attaches to the NDI preference issue. The dissolution of this high level group ended a dialogue that at least recognized the importance of the issue (even if no substantive action was taken) and sent a clear message to the acquisition community that NDI is no longer on the front burner.

DOD Letter:

"g. The Defense Systems Management College (DSMC), the principal training center for DoD program managers, has begun offering modules on NDI acquisition in each of their courses. Under current status, while the segment of instruction specifically dedicated to NDI is limited in scope and duration, as pointed out in the GAO report of Februaru 1989, consideration of NDI alternatives is an integral part of the case study which runs throughout the program managers course. Additionally, several other training courses now include segments on NDI acquisition."

Subcommittee Staff Comments:

Approximately 40 minutes out of the 20-week program managers course is dedicated to NDI. The two other courses offered at DSMC to acquisition personnel have insignificant time dedicated to NDI.

In a 28 July 1987 memorandum, the Undersecretary of Defense (Acquisition) asked DSMC to conduct a series of workshops at DSMC regional training centers. The workshops were to include case studies, cost/performance tradeoffs, logistical support, standardization, spares availability considerations, and specification techniques which would provide for NDI solutions, and contracting techniques that would encourage the use of NDIs.

We understand that the workshops were never conducted. The failure to conduct the workshops is significant in that they represent the only vehicle for training the majority of personnel who are not scheduled to attend formal courses at DSMC.

DOD Letter:

"h. A full-time position was established on the OSD staff in December 1986 to encourage use of NDI and advocate policy and procedural changes to increase NDI acquisition. The position was created and filled."

Subcommittee Staff Comments:

What actually happened is the two people at OSD working on the NDI initiative were reduced to one, and then the remaining person's time was split between NDI and other issues. The person at OSD has an industrial engineering background with approximately 17 years experience with specifications and standards. There is no one in DoD dedicated to NDI with either a contracting or major system acquisition background. Unlike TQM and industrial base projects, which have five or more people in the Pentagon plus DLA support personnel assigned, the NDI initiative has one half of one person. We understand that a second individual has been hired to assist on the NDI program within the last month.

DOD Letter:

"2. Additional actions that have been taken to implement Section 907 since 1987 are described in the report to Congress on "Simplification and Streamlining of Acquisition Procedures" and the report to the Secretary of Defense on "Enhancing Defense Standardization." Specific areas that impact DoD's ability to buy NDI include, from the Simplification and Streamlining of Acquisition Procedures report:

". the Pilot Contracting Activities Program;

". the Bank Card Program;

". Output from the DoD Contract Simplification Workshop;

". Clarification of when to obtain cost or pricing data;

"and from the Enhancing Defense Standardization report:

". the review of specifications and standards;

". suspension of issuance or revision of military specifications in 400 (of 657) federal supply classes;

". increased reliance on non-governmental standards."

Subcommittee Staff Comments:

GAO addressed the Pilot Contracting Activities Program in their report on DoD's efforts to promote NDI acquisition. DoD established the Pilot Contracting Activities Program as an attempt to increase individual authority by encouraging DoD contracting personnel to identify regulations, clauses and procedures that may be inappropriate and providing a means to obtain approval not to use them. As of September 1988, 450 requests for deviations or waivers had been received; however, according to DoD, these requests have been relatively minor in scope.

The guidance clarifying when to obtain cost or pricing data was issued in the form of a memorandum to the services and defense agencies on May 1, 1987. While the guidance is on point, it would have had a greater impact on the acquisition community if it had been issued as a change to the DoD FAR supplement at some time between May 1987 and the present.

A reading of the descriptions of the Pilot Contracting Activities Program, the Bank Card Program, and Contract Simplification Workshop fails to establish a connection with the NDI issue.

On the other hand, the effort DoD has expended in the area of specifications and standards should have a positive effect on the NDI issue.

DOD Letter:

"3. For each impediment identified in the 1987 report, actions taken to remove the impediment are as follows:

"a. Impediment #1: Contracts for nondevelopmental items include unnecessary clauses and there are too many and too complex regulations."

Refer to the DoD letter for actions since 1987.

Subcommittee Staff Comments:

DoD has not developed a standard, simplified contract for commercial or nondevelopmental items, which is the obvious answer to the problem of overly complex contract terms and conditions and inappropriate/inconsistent use of contract clauses.

The Subcommittee staff recently conducted a review of the contract clauses included in six separate DOD solicitations for the commercial purchase of oscilloscopes -- an instrument for measuring variations in electrical current. The staff found that 171 different contract provisions were included in at least one of the six solicitations. Of these contract clauses, only 27 were included in all six of the solicitations and only 57 were included in more than half of the solicitations. The staff's conclusion is that there is significant lack of consistency in the clauses that are included in the contracts for this commercial product.

DoD has indicated that it supports the OFPP draft bill on commercial acquisition. This bill, if enacted, would simply exempt commercial contracts from all contract clauses, whether statutorily or regulatorily mandated. The OFPP bill does not address nondevelopmental items that are not commercial.

DoD mentions under this impediment that the services and DLA have reduced by 30 percent the line count of their respective supplements to the FAR. While the reduction of unnecessary regulatory provisions is a worthwhile project and should be continued, there is no direct connection between this effort and the acquisition of NDI's.

DOD Letter:

"b. Impediment #2: Cost Accounting Standards (CAS) are an impediment to getting companies into the defense business."

Refer to the DoD response for actions since 1987.

Subcommittee Staff Comments:

The DoD response states that the OFPP Act Amendments of 1988 which reestablished the CAS board and raised the threshold from $100,000 to $500,000 for CAS application of the standards to negotiated contracts. The DoD response indicates that the higher threshold should reduce the incidence of CAS being an impediment to the acquisition of NDIs. This action was taken by the Congress, with DOD's support.

DOD Letter:

"c. Impediment #3: Government requirements for rights in technical data differ significantly from normal practices in the private sector."

Refer to the DoD response for actions since 1987.

Subcommittee Staff Comments:

The DoD response mentions the newly revised DoD supplement which limits the government's authority to require that contractors sell or relinquish their proprietary rights in technical data as a condition for award of a government contract. The response does not mention the numerous statutory directives that were necessary before these changes were made. DoD's revised rules appear to have addressed many of the problems associated with rights to technical data.

DOD Letter:

"d. Impediment #4: There are some rules for participation in the GSA multiple award schedule which discourage qualified offerors from participating."

Refer to the DoD response for actions since 1987.

Subcommittee Staff Comments:

DoD's response does not address the following problems related to the GSA Multiple Award Schedule that were raised in their 18 December 1987 report to Congress:

(1) A requirement for most favored pricing when the government is not necessarily a favored customer.

(2) A price reduction clause which requires extensive record keeping.

(3) Maximum order limitations that do not reflect quantify price break-point.

(4) Government access to records and data.

Instead, DoD talks about revised DoD regulations which have (i) eliminated the requirement to recompete items on the GSA schedules, and (ii) converted GSA schedules from mandatory to optional use. While helpful to some extent, neither of these two actions addresses the problems raised in DOD's draft report.

Another problem that the Subcommittee is aware of is the failure on the part of many contracting officers to accept products on the GSA schedules as commercial products. Contracting officers often require contractors to submit Form 1412 (Claim for Exemption from Submission of Certified Cost or Pricing Data) in order to establish commerciality of products that are on the GSA schedule. Similar information is required by GSA before the item is placed on the schedule. In short, the contractor is required to prove commerciality twice: first to get the product on the GSA schedule and then to sell it to DoD.

DOD Letter:

"e. Impediment #5. The Truth-In-Negotiation Act serves as an impediment, in some cases, to NDI acquisition. Under Actions since 1987, in addition to the actions identified in the report to Congress, DASD(P) has recently drafted a proposed revision to the regulations which applies to established catalog or market prices of commercial items sold in substantial quantities to the general public. The proposed change will streamline and simplify current requirements for determining when to request cost or pricing data, yet still be in compliance with the Truth-In-Negotiations Act. The draft is currently being reviewed by a small number of government and industry representatives. After evaluating comments received from that group, a case will be submitted to the DARC for consideration."

Subcommittee Staff Comments:

The draft change to the regulations addresses the principal problems related to catalog and market pricing of commercial products. These problems have been well known by DoD and industry for many years, yet nothing of any significance has been done by DoD to even address them, much less solve them, that is, until the appearance of this draft revision, which was prepared within the last month or two. Further, the mere emergence of this draft revision to the regulations is no guarantee that anything at all will actually be changed.

If the draft receives a favorable initial review, a formal DAR case will be established and processed. If the DAR case is processed in the normal manner, it will take about 16 months before revised regulations are actually published. It is also important to note that this average does not include the many DAR cases that never reach the end of the process; some problems are just too hard to solve.

DOD Statement:

4. Paragraph 4 of the DoD response contains a statement that ". . . DoD efforts have been directed toward removing or ameliorating the impact of previously identified impediments, and toward development of plans for improving our ability to buy NDI and to use commercial buying practices when it makes sense to do so."

Subcommmittee Staff Comments:

DoD's statement that it is encouraging the use of commercial buying practices is questionable. Commercial buying practices encompass the following:

a. The customer relies on the contractor to perform quality inspections and to supply a quality product.

b. The customer has a right to inspect the product prior to acceptance.

c. The contracting instrument is simple; terms and conditions consistent with the UCC are usually incorporated.

d. Customers use nongovernment standards and specifications that address form, fit, and function to describe their needs.

e. Contract award is normally based on "best value," rather than lowest initial cost.

f. Customers normally rely on and take advantage of product warranties.

g. Customers normally rely on product history and contractor recommendations in determining provisioning requirements.

h. Customers normally rely on contractor maintenance facilities and distribution channels.

DoD has made some progress with performance specifications; however, there is little real progress in promoting the use of other commercial buying practices.

DEPARTMENT OF THE ARMY
OFFICE OF THE UNDER SECRETARY
WASHINGTON, D.C. 20310-0102

20 April 1989

Honorable Carl Levin
Chairman
Subcommittee on Oversight
  of Government Management
United States Senate
Washington D. C. 20510-6250

Dear Mr. Chairman:

This letter responds to your March 23, 1989, letter requesting information on how the Army is implementing Section 907 of the National Defense Authorization Act for Fiscal Year 1987. Section 907 establishes a preference for purchases of nondevelopmental items (NDI). I am pleased to have this opportunity to provide you with an update on how the Army is doing on NDI.

The Army is pleased to note that it is the lead service in terms of completing NDI acquisitions. During a briefing to a member of your staff in February 1989, we pointed out that more than 30% of our combat and tactical systems procurements were NDI, as were about 95% of all information systems procurements. We also stated that the draft DOD Directive 5000.37 "Acquisition & Logistics Support of NDI" was modeled after the Army's NDI Handbook.

Detailed responses to your specific questions are contained in the following attachments:

Attachment 1 is a listing of all Army regulations, directives, guidelines, and manuals regarding the purchase of NDI.

Attachment 2 describes Army training programs, to include DoD schools that provide NDI exposure to our procurement and acquisition personnel. Specifically requested information such as the length of training and copies of course curriculum is included.

In response to the question, "Does the Army have any staff dedicated to the implementation of Section 907?", the answer is that we do have staff responsible for implementing Section 907, although I am not aware that any single person dedicates all of his or her time to that task. The Army has established a network of streamlining advocates at all U. S. Army Materiel Command (AMC) subordinate commands and the Information Systems Command under the general guidance of the Army's Streamlining Advocate, Mr. Robert Black of AMC. Their activities include reviewing all assigned programs and ensuring that NDI has been properly considered and that Section 907 is being implemented.

I believe that the Army has an excellent track record regarding the acquisition of NDI and we will continue to apply streamlining strategy for future procurements.

I trust this information will be useful.

Sincerely,

Michael P. W. Stone
Under Secretary of the Army

Analysis of Army's Response to Senator Levin's Inquiry of DoD Actions to Promote Acquisition of Nondevelopmental Items

June 1, 1989

a. The Army Provided copies of the following regulations:

(1) AR 25-1, Army Information Resources Management program. This publication states that (i) Commercially available or government owned items will be used in information systems when possible, consistent with design, operational, logistics, and security requirements.

(2) AR 70-1, Systems Acquisition Policy and Procedures. This publication addresses categories of NDI, market research, performance specifications and a two-step sealed bidding process to acquire NDIs.

(3) AR 602.2, Manpower and Personnel Integration (MANPRINT) in Material Acquisition Process. This publication mentions that MANPRINT considerations must influence selection of the basic nondevelopmental item (NDI) or components to be assembled, the design of any modification and the integration hardware and software.

(4) AR 700-127, Integrated Logistics Support. This publication contains a section on ILS management for nondevelopmental item acquisitions.

b. The Army provided copies of the following draft regulations:

(1) AR 70-XX, Research, Development, and Acquisition Test and Evaluation. This publication has a section on Test and Evaluation (T&E) of NDIs. NDI systems are required to undergo technical and operational T&E prior to the procurement decision, unless a definitive decision is made by the decision authority that previous testing or other data (such as user/market investigations) provide sufficient evidence of acceptability.

(2) AR 70-XX, Research, Development, and Acquisition of International Nondevelopmental Items (INDI). This publication extends the preference for NDIs to systems, subsystems, components and munitions developed or being developed by allied countries.

c. The Army provided copies of the following pamphlets:

(1) DA Pam 70-2, Material Acquisition Handbook. This comprehensive publication is the equivalent of the Navy's NDI manual. It is currently being upgraded from a

AMC/TRADOC pamphlet to an Army pamphlet; scheduled publication date is November 1989.

(2) DA Pam 70-21, A Test and Evaluation Guide. This publication contains a section on NDI testing and NDI life cycle procedures.

(3) The Army provided a revised copy of AMC Regulation 700.15, Integrated Logistic Support, which is scheduled to be published in June 1989. This publication has a chapter on NDIs that deals with market investigation and analysis; commercial manuals for NDIs; and nondevelopmental test, measurement, and diagnostic equipment.

d. The Army provided the following information related to training in NDI:

(1) Army Logistics Management School (ALMC):

(a) Material Acquisition Management Course: Length: 9 weeks; NDI: 2 hrs; 290 students/yr

(b) Defense Specification Management Course: Length: 2 weeks; NDI: 1-hr lecture & 2-hr practical exercise on CIDs; 300 students/yr

(c) Defense Specification Users Course: Length: 1 week; NDI: 1 hr: 350 students/yr

(d) Integrated Logistics Support Course: Length: 2 weeks; NDI: discussed as part of the acquisition process; 280 students/yr

(e) Reliability Centered Maintenance: Length: 1 week; NDI: discussed as part of the acquisition process; 200 students/yr

(2) Army Management Engineering College (AMEC): The Army identified 13 courses (average length: 2 weeks) during which NDI is discussed as part of the acquisition process.

(3) Defense Systems Management College (DSMC):

(a) Program Management Course: Length: 5 months; NDI: 40 Min; 163 students/yr (there is also a rather lengthy case study that deals with NDI)

(b) Fundamentals of Systems Acquisition: Length: 1 week; NDI: 15 min; 109 students/yr

(4) HQ AMC Army Streamlined Acquisition Program: Length: 1 week; NDI: 6 hrs/case studies; 200 students/yr

e. The Army stated that no single person dedicates all of his or her time to NDI. The Army has assigned NDI responsibility to its streamlining advocates, who are located at all AMC subordinate commands and the Information Systems Command. Streamlining advocates review all assigned programs and ensure that NDI has been properly considered and that the statutory preference for NDI has been implemented.

From the above information, it appears that the Army is trying to institutionalize the preference for NDIs in its regulations and in its formal training program.

As for the acquisition streamlining network, the Army provided a list of 15 streamlining advocates (Encl 1). The Army also provided the following three documents that relate to the function of the NDI/Streamlining advocates:

(1) Message to Army commands from the commanding general, AMC, Subject: NDI Policy, dated 19 Dec 85. The message establishes an NDI advocate at each command. The NDI advocate is, among other things, to track actual NDI experience so that progress, savings in time and cost, and lessons learned can be identified.

(2) Letter to Army commands from HQ, AMC, subject: NDI advocate responsibilities, dated 20 Jun 86. This letter outlines the duties of the NDI advocate and emphasizes their importance. The NDI advocate is to track NDI progress as follows:

(a) Identification of all systems in each command, to include the NDI systems fielded.

(b) time and cost savings must be identified.

(c) Lessons learned on NDI are to be documented.

(3) Message to Army commands from the commanding general, AMC, subject: Army Streamlining Advocate Role, dated 30 Dec 86. This directive abolishes the NDI advocate as a separate entity, and combines this function with the streamlining advocate function. Among the duties of the streamlining advocate is to "steer taskings and consolidate inputs on the various aspects of streamlining (including tracking of ASAP/NDI systems performance)." ASAP means Army Acquisition Streamlining Program.

ACQUISITION STREAMLINING ADVOCATES

COMMAND	ADVOCATE/ALTERNATE	OFFICE SYMBOL	PHONE # AV & COMM	DATAFAX #
AMC				
AMCCOM	Robert J. Radkiewicz/ Chuck Burgner	AMSMC-RT	AV 793-4551 (309) 782-4551	(309) 782-3296/ 7332
AVSCOM	David J. Weller/	AMSAV-N	AV 693-1070 (314) 263-1070	(314) 263-1326
	Joseph C. Marlo	AMSAV-NR	AV 693-1082	
CECOM	Richard J. Caccamise/	AMSEL-PL	AV 992-4502 (201) 532-4502	(201) 532-3420
	Nancy Roberts	AMSEL-PL-PA	AV 992-1880/ 1879/8523	
DESCOM	A. J. Meyer	AMSDS-FM-L	AV 570-5213/ 5218 (703) 267-5213	(717) 267-9845
LABCOM	Kevin E. Kirby	AMSLC-CT	AV 290-4486 (202) 394-4486	(202) 394-4889
MICOM	Harry E. Cook (Actg.)	AMSMI-OR	AV 746-4414 (205) 876-4414	(205) 876-1801
	John Daly		AV 746-5815	
TACOM	Douglas B. Munro/	AMSTA-CM	AV 786-6113 (313) 574-6113	(313) 574-5952
	MAJ Peter G. Tuttle	AMSTA-ZDS	AV 786-5061	
TECOM	Todd E. Stevenson (On detail to DACS-TE, 695-8995)	AMSTE-TA-0	AV 298-4544 (301) 278-4544	(301) 278-7653 Pent. detail- 695-9127
TROSCOM	Allen C. Christensen	AMSTR-E	AV 693-2734 (314) 263-2734	(314) 263-1537
AMSAA	Dave Gilbert	AMXSY-D	AV 298-4919/6607 (301) 278-4919	(301) 278-6242
COE	Rodger Seeman	CEEC-ES	(202) 272-1185	(202) 272-0682
ISC	Feliciano Giordano	ASQM-D	AV 992-7960/64 (201) 532-7960	(201) 532-7919
OTEA	Fred McCoy	CSTE-PO-PP	(703) 756-1821	(703) 756-
TRADOC	COL Dan Stephenson	ATCD-E	AV 680-4162/2744 (804) 727-4162	(804) 727-3614
TSG	MAJ George Hammel	DASG-HCL-S	(703) 756-8060	(703) 756-0243

DEPARTMENT OF THE NAVY
OFFICE OF THE SECRETARY
WASHINGTON, D.C. 20350-1000

25 April 1989

The Honorable Carl Levin
Chairman, Subcommittee on Oversight
of Government Management
Committee on Governmental Affairs
United States Senate
Washington, D.C. 20510-6250

Dear Mr. Chairman:

The following is our response to your request of March 23, 1989, for information on the Department of the Navy's Non-Developmental Item Program (NDI).

The two principal NDI documents are the Secretary of the Navy Instruction 4210.7A of January 16, 1987 (TAB A) on "Effective Acquisition of Navy Material," and the Non-Developmental Item Acquisition Handbook NAVSO P-3656 of June 6, 1988 (TAB B). The instruction had a distribution of 250. However, with local reproduction it is impossible to estimate the total copies now in existence. We printed 2,700 copies of the Handbook. These were distributed to our acquisition commands and used as handouts in our Acquisition Streamlining Course.

We address NDI in two Department of the Navy acquisition training courses. The first is our Acquisition Streamlining Course, a 20 hour course that has been conducted for the last three years. NDI has been integrated into the acquisition streamlining process and is 25-30 percent of the course. TAB C is the course curriculum. To date, we have had 2,600 students. The other course is the Navy Systems Acquisition Management Course, a 40 hour course on the acquisition process. In the one and one-half hour block of instruction on acquisition streamlining, 15 minutes is devoted to NDI. This course curriculum is at TAB D. Since introducing the module, we have had 1,200 students.

There is no solely dedicated NDI staff within the Department of the Navy. The NDI program is integrated into acquisition streamlining and is under our Streamlining Advocates. There are Streamlining Advocates in the Department of the Navy's Specification Control Advocate General's Office and in our major acquisition commands. They assist program and acquisition managers in streamlining programs and review acquisition plans to ensure programs are being streamlined including the use of NDI solutions.

The Department of the Navy integrated six improvement programs under the initiative ACTION '88, now ACTION PLUS. NDI is one of these programs. TABS E through H provide literature relating to this initiative. ACTION '88 included awareness presentations given to the major acquisition command executives by upper level Department of the Navy officials.

I hope this material meets the needs of your committee and will provide you with an insight to the Department of the Navy's NDI efforts. As always, if I can be of any further assistance, I hope you will not hesitate to contact me.

Sincerely,

H. Lawrence Garrett, III
Secretary of the Navy
Acting

TAB A - SECNAVINST 4210.7A of 16 Jan 87
TAB B - ASN(S&L) memo of 10 Jun 88
TAB C - NDI portion of DON Acquisition Streamlining Course
TAB D - NDI portion of Navy Systems Acquisition Management Course
TAB E - ACTION PLUS Brochure
TAB F - ACTION PLUS Flier
TAB G - UPDATE of Mar/Apr 89
TAB H - Acquisition Streamlining Brochure

Analysis of Navy's Response to Senator Levin's Inquiry of DoD Actions to Promote Acquisition of Nondevelopmental Items

June 1, 1989

Each paragraph of the Navy's response is quoted and commented on by the Subcommittee staff:

a. The two principal NDI documents are the Secretary of the Navy Instruction 4210.7A of January 16, 1987 (TAB A) on "Effective Acquisition of Navy Material," and the Nondevelopmental Item Acquisition Handbook NAVSO P-3656 of June 6, 1988 (TAB B). The instruction had a distribution of 250. However, with local reproduction it is impossible to estimate the total copies now in existence. We printed 2700 copies of the Handbook. These were distributed to our acquisition commands and used as handouts in our Acquisition Streamlining Course.

Subcommittee Staff Comments:

(1) The first document is a high-level policy document that is very comprehensive and positive in its treatment of the statutory preference for acquisition of NDIs. It provides an excellent framework for a model NDI program. The question we need to delve into is to what extent is it being implemented. Paragraph 7 (Requirements and Responsibilities) contains the following provisions that, upon further inquiry, may help us answer this question:

(a) "The Navy Specification Control Advocate General shall function as the Navy NDI Advocate. The advocate will monitor NDI related activities of the Marine Corps, Systems Commands and Program Managers and report to the Secretary of the Navy on the effectivness of these activities."

(b) "The Commandant of the Marine Corps, Systems Commanders and Program Managers are responsible for the timely and successful implementation of the NDI initiative within their respective commands. This responsibility shall include the following actions: . . . (5) Report overall progress in promoting and using NDI as part of the semiannual flag level review of acquisition streamlining."

(c) "Space and Naval Warfare Systems Command (SPAWARSYSCOM) shall serve as the leading SYSCOM. In this capacity SPAWAR will: (1) Prepare NDI acquisition guidance for use by program managers in the selection, procurement, qualification and test and effective operational support of NDI."

I think we should ask the Navy if the above provisions are being complied with. If so, then we should ask for documentation which substantiates such compliance. The documentation we would need would be (i) the most recent report from the Navy NDI Advocate to the Secretary of the Navy, (ii) the most recent progress reports from the Commandant of the Marine Corps, Systems Commanders, and Program Managers that were rendered as part of the semiannual flag level review of acquisition streamlining, and (iii) the guidance that was prepared by SPAWAR for use by program managers.

Answers to the above questions will shed light on how well the Navy's NDI program is being managed.

(2) The Navy's NDI Handbook is a very comprehensive document that addresses all aspects of the acquisition of NDIs. The Navy should be commended for this effort.

b. We address NDI in two Department of the Navy acquisition training courses. The first is our Acquisition Streamlining Course, a 20-hour course that has been conducted for the last three years. NDI has been integrated into the acquisition streamlining process and is 25-30 percent of the course. TAB C is the course curriculum. To date, we have had 2,600 students. The other course is the Navy Systems Acquisition Management Course, a 40-hour course on the acquisition process. In the one and one-half hour block of instruction on acquisition streamlining, 15 minutes is devoted to NDI. This course curriculum is at TAB D. Since introducing the module, we have had 1200 students.

Subcommittee Staff Comments: NDI apparently represents a significant part of the 20-hour Acquisition Streamlining Course. However, in the Navy Systems Acquisition Management Course, 15 minutes or NDI out of 40 hours is insignificant.

c. There is no solely dedicated NDI staff within the Department of the Navy. The NDI program is integrated into acquisition streamlining and is under our streamlining advocates. There are streamlining advocates in the Department of the Navy's Specifications Control Advocates General's Office and in our major acquisition commands. They assist program and acquisition managers in streamlining programs and review acquisition plans to ensure programs are being streamlined including the use of NDI solutions.

Subcommittee Staff Comments: The above statement is consistent with the provisions of SECNAV Instruction 4210.7A (Effective Acquisition of Navy Material).

d. The Department of the Navy integrated six improvement programs under the initiative ACTION 88, now ACTION PLUS. NDI is one of these programs. TABS E throuth H provide literature relaing to this initiative. ACTION 88 included awareness presentations given to the major acquisition command executives by upper level Department of the Navy officials.

Subcommittee Staff Comments: The documentation provided by the Navy substantiate that NDI is addressed under the initiative ACTION 88, now ACTION Plus.

DEPARTMENT OF THE AIR FORCE
WASHINGTON, D.C. 20330-1000

OFFICE OF THE SECRETARY

APR 25 1989

The Honorable Carl Levin
Chairman, Subcommittee on Oversight
of Government Management
Committee on Governmental Affairs
United States Senate
Washington, D. C. 20510-0001

Dear Mr. Chairman:

This is in response to your letter of March 23, 1989, to the Assistant Secretary of the Air Force regarding Section 907 of the National Defense Authorization Act for Fiscal Year 1987 concerning nondevelopmental items (NDIs). Our response addresses your specific questions and provides a view of what is needed.

The following regulations (see attachments) contain policy on selecting and purchasing commercial products and other previously developed item (Air Force and NATO).

a. AFP 800-41, "Selling to the United States Air Force." This provides the commercial sector information on what products are being procured by the Air Force and identifies cognizant Air Force activities. (Attachment 1)

b. AFR 800-2, "Acquisition Program Management." This is the Air Force's principal systems/equipment acquisition policy. It implements DoDD 5000.2, "Major System Acquisition Procedures," which in turn implements DoDD 5000-.37, "Acquisition and Logistics Support of Nondevelopmental Items (NDI)." (Previously provided.)

c. AFR 800-12, "Acquisition of Support Equipment." This states NDI preference policy regarding the selection and acquisition of support equipment. (Previously provided.)

d. AFR 800-14, "Lifecycle Management of Computer Resources in Systems." This provides policy on acquiring commercial off-the-shelf (COTS) computer resources. (Attachment 2)

e. AFR 800-22, "CFE vs GFE Selection Process." This establishes a process for selecting previously developed/ commercial equipment instead of developing new items. Implementing command regulations establishes a Standard/Preferred Items List for procuring activity use. (Attachment 3)

f. AFR 800-24, "Parts Control Program." This establishes a process requiring the selection of inventory (standard) parts during the design of developmental items. (Attachment 4)

g. DRAFT AFR XXXX, "Foreign Weapons Evaluation (FWE) and NATO Comparative Test (NCT) Program" (estimated publication - July 1989). Implements DoDD 5000.3-M-2, "Foreign Weapons Evaluation and NATO Comparative Test Programs," and establishes a process for evaluating previously developed foreign equipment as candidates for competitive Air Force procurements. (Attachment 5)

h. DRAFT AF GUIDE, "Commercial Equipment Acquisition." This provides COTS selection and acquisition decision criteria. (We have provided it for inclusion in the draft DoD NDI Acquisition Manual and provided it to Air Force acquisition activities for use in draft form. Formal issuance is expected by June 1989 if the DoD manual is not published.) (Previously provided.)

i. AFR 57-4, "Modification Approval and Management." Modifications to commercially available computer resources (paragraph 2.1) and the need for expeditious action by Configuration Control Boards reviewing commercially offered modification (paragraph 14.c) are NDI related procedures addressed in this regulation. (Attachment 6)

j. AFR 700-1, "Managing Air Force Communications-Computer Systems." (Attachment 7)

k. AFR 700-3, "Communications-Computer Systems Requirements Process." (Attachment 8)

l. AFR 700-4, Vol I, "Communications-Computer Systems Program Management and Acquisition." (Attachment 9)

m. AFR 700-4, Vol II, "Information Systems Program Management and Acquisition." (Attachment 10)

n. Air Force Policy on Programming Languages, AF/CVA Letter, November 9, 1988. (Attachment 11)

o. Air Force Planning and Architecture Guidance, Part I, February 1989. (Attachment 12)

p. Air Force Planning and Architecture Guidance, Part II, September 1988. (Attachment 13)

q. Air Force Information Systems Architecture, Vol I, May 8, 1985. (Attachment 14)

r. DFAR 210.001 and .002. (Attachment 15)

s. Air Force Acquisition Streamlining and Standardization Training Course program plan. (Attachment 16)

The attached program plan (Attachment 16) outlines an Air Force Acquisition Streamlining and Standardization Training Course patterned after similar Navy and Army training courses which includes coverage on acquisition of nondevelopmental items. Due to O&M funding constraints, the Air Force course has not yet been initiated. Further training requirements will be considered during a June 1989 conference which will change the current proposed course to not only address the preference for NDI and potential benefits but also provide NDI acquisition and management guidance.

NDI is a part of the Air Force's Departmental Standardization Office. Approximately 400 staff hours have been spent on NDI policy and procedures and meetings concerning the impact and implementation of the NDI legislation.

The principal efforts have been to prepare and field the Air Force "Commercial Equipment Acquisition" guide and to advocate the need for a joint DoD wide integrated effort to promote NDI acquisition. Due to the range, scope and impact of the NDI legislation, we believe that a DoD wide structure of policy, procedures and data bases is needed to enhance NDI acquisitions. This should be done with existing resources and not by creating new offices.

As evidenced by the regulations cited in Section 1, the Air Force has been encouraging the use of NDI even before NDI legislation was passed.

An Air Force conference is planned to disseminate information on NDI acquisition and to discuss associated support issues and problems which will help formulate NDI selection and acquisition procedures.

We hope you find this information helpful. Please contact us if we can be of further assistance in this matter.

Sincerely,

Harold R. Denman

HAROLD R. DENMAN
Colonel, USAF
Program Liaison Division
Office of Legislative Liaison

Attachments

Analysis of Air Force's Response to Senator Levin's Inquiry of DoD Actions to Promote Acquisition of Nondevelopmental Items

June 1, 1989

1. Overall Impression of Air Force Response: The Air Force has provided copies of regulations which are generally not very supportive of NDI purchases. Some of the regulations take a very negative view toward NDIs with an implicit preference for Mil-Spec items. The failure to provide training is blamed on the O&M funding shortage (Congress' fault) rather than their lack of initiative in this area. Further, what is really significant is that the Air Force did not refer to any provision in the basic Air Force Supply Regulation, AFR 67-1. This is the regulation to which one refers for guidance in how to get an item for Air Force use.

2. The paragraph designations that follow are the same as in the USAF letter dated April 25, 1989. The analysis of each section follows the quoted material from the Air Force's letter dated April 25, 1989.

a. AFP 800-41, "Selling to the United States Air Force." This provides the commercial sector information on what products are being procured by the Air Force and identifies cognizant Air Force activities.

Analysis: This document identifies the purchasing offices and the Federal Stock Classes for items purchased by these offices. This document may be useful to a supplier not accustomed to doing business with the Air Force but does nothing to make the purchase of commercial items more likely.

b. AFR 800-2, "Acquisition Program Management." This is the Air Force's principal systems/equipment acquisition policy. It implements DoDD 5000.2, "Major System Acquisition Procedures," which in turn implements DoDD 5000.37, "Acquisition and Logistics Support of Nondevelopmental Items (NDI)."

Analysis: There is no mention of NDI's in this regulation. The only mention of Commercial items is that DoDD 5000.37, "Acquisition and Distribution of Commercial products (ADCoP)," September 29, 1978, is listed in the references section of DoDD 5000.2 which is attached to AFR 800-2. The Air Force regulatory language which, according to the Air Force, is "the Air Force's principal systems/equipment acquisition policy," does not mention NonDevelopmental Items nor does it mention commercial items.

c. AFR 800-12, Acquisition of Support Equipment," This states NDI preference policy regarding the selection and acquisition of support equipment.

Analysis: The only mention of Commercial items appears in paragraph 3. c. where "Commercially available items that meet technical and logistics requirements" is listed as the fourth of six categories. The order of preference is listed as follows:

(1) Standard item.
(2) Preferred item.
(3) Items in the government inventory or being developed under government contract.
(4) Commercially available items that meet technical and logistics requirements.
(5) Modification of any of the above.
(6) Newly developed items.

The second item in the foregoing list is not defined so we cannot tell what is intended. This skimpy mention in a seven page regulation, the most of which is directed at the procedure to be followed by the Air Force in approving and testing the contractor's recommended item of support equipment. There is no evidence that the preference for NDIs or commercial items is expressed in contractual terms to the prime or developing contractor who is responsible for identifying support equipment requirements.

d. AFR 800-14, "Lifecycle Management of Computer Resources in Systems." This provides policy on acquiring commercial off-the-shelf (COTS) computer resources.

Analysis: The policy concerning commercial computer resources is found on page 10 of 40 pages and does not express a preference for such resources. The balance of the regulation seems to be directed to actions which do not use commercial computer resources (hardware and software).

e. AFR 800-22, "CFE vs GFE Selection Process." This establishes a process for selecting previously developed/commercial equipment instead of developing new items. Implementing command regulations establishes a Standard/Preferred Items List for procuring activity use.

Analysis: This regulation which was issued in August, 1976, expresses some preference for commercially available items, listed 3rd of 5 items. This certainly was not done in response to the statutory requirement enacted in October 1986.

f. AFR 800-24, "Parts Control Program" This establishes a process requiring the selection of inventory (standard) parts during the design of developmental items.

Analysis: According to DoD and DLA the Parts Control Program is not related to the NDI issue!

g. DRAFT AFR XXXX, "Foreign Weapons Evaluation (FWE) and NATO Comparative Test (NCT) Protram" (estimated publication - July 1989). Implements DoDD 5000.3-M-2, "Foreign Weapons Evaluation and NATO Comparative Test Programs," and establishes a process for evaluating previously developed foreign equipment as candidates for competitive Air Force procurements.

Analysis: It is interesting that this regulation which implements the Nunn Amendment to the DOD Authorization Act of 1986 provides a mechanism to evaluate and possibly purchase NDI's from NATO (foreign) firms when we see evidence that it is so extremely difficult for our domestic commercial firms to do business with the Air Force. It should be noted that most of the statutory socio-economic provisions do not apply to foreign firms.

h. DRAFT AF GUIDE, "Commercial Equipment Acquisition." This provides COTS selection and acquisition decision criteria. (We have provided it for inclusion in the draft DoD NDI Acquisition Manual and provided to Air Force Acquisition activities for use in draft form. Formal issuance is expected by June 1989 if the DoD manual is not published.)

Analysis: The tone of the draft guide is very negative. The guide was issued in July, 1988, to Air Force Logistics Command, Air Force Systems Command and Air Force Communications Command with instructions to "issue it to all your acquisition and procurement activities for their use and review." They do not know how many nor to whom copies were actually distributed. If this is the only guidance published there is not likely to be any increase in the Air Force use of NDIs. The draft does not address the issue of using commercial items (usually component level) in the design and production of weapon systems. There is probably more opportunity in this area than in any other for the use of NDIs.

i. AFR 57-4, "Modification Approval and Management," Modifications to commercially available computer resources (paragraph 2.1) and the need for expeditious action by Configuration Control Boards reviewing commercially offered modification (paragraph 14.c) are NDI related procedures addressed in this regulation.

Analysis: The two cited brief mentions of commercial items relate only to computers and aircraft. Neither provision is useful in terms of NDI acquisition nor modification. The first instance (2.1) concerns the modification of Automatic Data Processing Resources and simply refers to the regulations to be followed. The second (14.c) is: "Expedite CCB actions on commercial off-the-shelf aircraft so the manufacturer receives notification, within the normal 30 calendar-day period, of Air Force action on the offered mods."

The balance of the regulation is generally directed to the modification of Mil-Spec equipment.

j. AFR 700-1, "Managing Air Force Communications-Computer Systems."

Analysis: This regulation is one of the maze of egulations which must be followed to acquire communications-computer equipment. Requiring activities must follow some or all of the Air Force 700 series regulations, 800 series regulations and the Federal Information Resources Management Regulations (FIRMR) which is maintained by the General Services Administration. Further, the Air Force regulations are supplemented at the Command and perhaps the local level.

In addition to these regulations the Federal Acquisition Regulation (FAR) and the supplements (DFARS, Defense Acquisition Regulation Supplement; and the AFFARS, Air Force Federal Acquisition Regulation Supplement must be followed when purchasing Communications-Computer Systems..

Not only are the cited provisions not particularly helpful, the proliferation of regulatory guidance in this area (computers and related equipment) makes it almost impossible for the professionals in the field to find the correct guidance. These regulations are not written to encourage the purchase of commercial equipment, they are written to describe the circumstances under which computer or communications may be purchased or leased.

k. through q. which consists of various regulations related to computers, such as AFR 700-3, "Communications-Computer Systems Requirements Process."

Analysis: (See comments for paragraph j.)

r. DFAR 210.001 and. 002.

Analysis: See analysis of DoD submission.

s. Air Force Acquisition Streamlining and Standardization Training Course program plan.

The attached program plan outlines an Air Force Acquisition Streamlining and Standardization Training Course patterned after similar Navy and Army training courses which includes coverage on acquisition of nondevelopmental items. Due to O&M funding constraints, the Air Force course has not yet been initiated. Further training requirements will be considered during a June 1989 conference which will change the current proposed course to not only address the preference for NDI and potential benefits but also provide NDI acquisition and management guidance.

Analysis: The management plan is a plan to hire a contractor to develop a three hour course for executives and a three and one-half day course for the working level. There are many existing courses into which material could and should be incorporated. Examples are: the basic course for contracting officers, Contract Cost/Price Analysis, the basic item management course and AFIT courses for Program Managers.

Further, if all the services are planning similar training, why is the Air Force waiting for O&M money to have the curriculum developed? Why is not DOD developing the course for all the services or if it is already developed by the Army or Navy, why is it necessary for the Air Force to pay for its development again?

B. MILITARY SPECIFICATIONS

Enhancing Defense Standardization

Specifications and Standards: Cornerstones of Quality

DEPARTMENT OF DEFENSE
UNITED STATES OF AMERICA

Report to the Secretary of Defense
by the Under Secretary of Defense (Acquisition)

November 1988

IV. ENHANCING DEFENSE STANDARDIZATION

The recommendations in this report, which have either been completed or are underway, are the result of input from participants from the Office of the Under Secretary of Defense (Acquisition), the Military Departments, and the Defense Logistics Agency who served on the Defense Standardization Study Team, as well as contributions from the Defense Standardization Council, the Departmental Standardization Offices, the Defense Science Board, industry associations, and non-Government standards bodies. Implementation of nearly all the recommendations is possible within the existing authority of the Department, but requires a political will and resource commitment that has been missing in the past. Since a few of the recommendations affect federal specifications and standards that are promulgated under the authority of the General Services Administration, their assistance is necessary for full implementation; as is the assistance of the National Institute of Standards and Technology of the Department of Commerce. Traditionally, both these organizations have been most cooperative, and we foresee no problem in obtaining their support.

"The recommendations in this report, . . . have either been completed or are underway. . ."

CONCLUSIONS AND RECOMMENDATIONS

The remaining portion of this section contains 12 conclusions and recommendations for action by the Department of Defense and other Government departments and agencies. The order of presentation generally corresponds with our six major thrusts: (1) establishing accountability within the Military Departments and Agencies for achieving program objectives; (2) conducting a comprehensive review of all specifications and standards to ensure they are in compliance with current Department of Defense policies; (3) establishing closer relationships with non-Government standards bodies and industry; (4) automating standardization data bases that serve as tools in the development, storage, retrieval, dissemination, application, and analysis of specifications and standards; (5) designating an executive agent to program and budget for special standardization projects; and (6) promoting expanded training for the developers and users of specifications and standards to effect the necessary cultural change.

Military Department and Agency Accountability

Conclusion

The Military Departments and Agencies do not have senior level standardization offices with enough authority and resources to enforce standardization document policy implementation, and there is little accountability.

Discussion

Department of Defense policies on specifications and standards are often times only paid *lip service* because each Military Department and Agency seems to lack an office with sufficient authority to enforce implementation of policy. Specification preparing activities are responsive to the goals set by their local commanders, and these do not necessarily support the corporate policy objectives, such as standardization. The excuse is frequently made that there are insufficient resources to implement policy. The resources are available, but as with all programs, there is fierce competition for those resources.

At present, the Departmental Standardization Offices for each Military Department and Agency are responsible for seeing that policies are implemented, and for translating policies into meaningful objectives for the individual activities within their component. The Departmental Standardization Offices are largely ineffective. They do not have enforcement authority, and their staffs are too small to work closely with their component activities to establish and monitor implementation of Military Department and Agency goals and objectives.

If we are to make significant improvements in our specifications and standards within a reasonable time frame, policies must be fully and rapidly implemented. To achieve this end, there must be authority and the political will to exercise that authority within each Military Department and Agency. The newly created Defense Standardization Council could provide the necessary authoritative leadership to ensure timely and thorough implementation of policies, but only if the members from each Military Department and Agency are in a position to mandate compliance.

"The Military Departments and the Defense Logistics Agency will each designate an office and a standardization executive. . ."

Recommendations

The Military Departments and the Defense Logistics Agency will each designate an office and a standardization executive with sufficient authority to mandate compliance with standardization policies and to commit resources to implement these policies. These offices will also be responsible for establishing a Military Department/Agency policy implementation plan, and for providing the Under Secretary of Defense (Acquisition) with progress reports. The Department of Defense directive that establishes policy for the Defense Standardization Program will be revised to recognize this new chain of responsibility officially.

Reviewing Specifications and Standards

Conclusion

While most specifications and standards are adequate to meet the needs of the Department of Defense, there are thousands of documents that are either overage, contain obsolete technical requirements, may no longer be needed, are in the wrong document series, or contain overly restrictive requirements. In nearly all cases, these shortcomings are the result of not complying with standardization policies intended to prevent such occurrences.

Discussion

Government specifications and standards have been criticized for being obsolete, overage, overly restrictive, and not conducive to commercial acquisition. While some of this criticism is unjustified or misdirected, there is ample room for improvement. A review of the *Department of Defense Index of Specifications and Standards* demonstrates there are about 7,200 overage documents for which appropriate corrective action has not been initiated; there are duplicative documents that could be combined or eliminated; there are military specifications and standards that could be replaced by non-Government standards or commercial item descriptions; there are several documents that have been in interim status for years and need to be fully coordinated; and there are many documents that have been improperly designated as specifications, standards, or some other type of document.

Program plans are an underutilized tool that can be used to plan for the replacement of Government documents with non-Government standards, the consolidation or elimination of duplicative documents, and to establish agreements for future document development. Program plans need to be better written, resources need to be committed to fulfill the commitments in the plan, and there must be continual monitoring by the lead standardization activities and the Departmental Standardization Offices to ensure implementation of the plan.

Military specifications should be used only to acquire items that have unique military applications. For items that are commercial products, non-Government standards, commercial item descriptions, federal specifications, and multiple award schedules should be the preferred acquisition vehicles.

Recommendations

"The Military Departments and Agencies will review each Government document. . ."

The Military Departments and Agencies will review each Government document for which they are the proponent to determine if the document: is current or in need of being updated; covers an obsolete item and should be canceled or inactivated for new design; describes a commercial product, and should be replaced by a non-Government standard, commercial item description, federal specification, or multiple award schedule; is in interim status and requires immediate coordination; duplicates existing documents and could be combined or eliminated; and is properly identified as a specification, standard, or handbook. Upon submission of this report, the Military Departments and Agencies will submit an action plan within 180 days to the Under Secretary of Defense (Acquisition) indicating corrective measures and milestones. Any Government document which has not been reviewed and appropriate action indicated will be canceled.

A change to the *Defense Standardization Manual* will be issued to improve the quality of program plans, and enlist the support of the members of the Defense Standardization Council to ensure the resources and commitment to implement the tasks in the plan.

A meeting with the General Services Administration will be arranged to discuss the effect of these recommendations on federal specifications and standards, and to seek authorization for the Department of Defense to cancel and supersede federal specifications and standards with their concurrence.

"All existing interim documents will be either canceled or coordinated immediately."

All existing interim documents will be either canceled or coordinated immediately. A sunset clause will be mandated to appear on all future interim documents that will automatically cancel the document at the end of two years.

Living Specifications

Conclusion

The present approach to developing military specifications is not always responsive to the user's needs, and does not encourage vendors to supply the most current state-of-the-art items. Supplying products to the traditional military specification requires only meeting the specified requirements, and there is little incentive to do better or to produce better quality products. Work needs to be done to develop a *living specification* that will be more flexible, more responsive to the user's needs, and more adaptable to changes in technology.

Discussion

In order to change the traditional approach to military specifications, we need to pursue the concept of a *living specification*, which is defined as a formatted document that allows for rapid insertion of new technology, permits the use of advanced manufacturing process techniques, and promotes continuous quality improvement without the need of major revisions or updates to the specification. *Living specifications* might assume a variety of appearances, such as a performance specification or a *fill-in-the-blank* guide specification.

We must avoid needlessly expanding the traditional quality control inspection program. We have a tendency to add more testing in order to correct various quality related problems. This approach has contributed to a decline in competitiveness. There is a need to seek out and correct the root cause of the problems, and to design and manufacture quality into the product. The *living specification* supports implementation of the Department's total quality management program that includes such tools as statistical process control for reducing reliance on end-of-line product inspection. Full implementation of the qualified manufacturers list program is essential to the *living specification* concept. This program will allow the Department to work with manufacturers and recognize their process capabilities through accreditation and certification, and rely on their certified manufacturing processes, provided the product conforms to the specified performance requirements.

It is recognized the *living specification* approach is not applicable in all cases, particularly in reprocurement specifications where exact design interfaces may be critical, but action needs to be taken to break free from past solutions that will no longer satisfy the user's needs in today's fast-moving, high-technology environment.

Recommendations

Each Military Department will identify 25 high-technology candidate specifications that will be revised under a pilot program to reflect the concepts of the *living specification*. The specifications generated under this pilot program can be used as models to create

"Each Military Department will identify 25 high-technology candidate specifications that will be revised under a pilot program to reflect the concepts of the living specification."

". . .policy for the establishment of qualified manufacturers lists will be developed, coordinated, and issued."

living specifications for other moderate to high technology commodities. In support of this action, policy for the establishment of qualified manufacturers lists will be developed, coordinated, and issued.

Non-Government Standards

Conclusion

There is much potential to increase the number of non-Government standards adopted by the Department of Defense to replace military specifications and standards. Greater reliance on non-Government standards would expand the Department's acquisition of commercial products and processes, thus saving money, reducing lead time, improving quality, and bolstering our defense industrial competitiveness.

Discussion

One major obstacle facing the Department of Defense in its efforts to adopt non-Government standards is the lack of product standards. Those non-Government standards bodies with which the Department is most involved support the idea of developing more product standards, but such standards are not being developed quickly enough for a number of reasons. Consistent participation by Department personnel on the technical committees that generate the standards is often limited because of restrictions on travel funds and because work on non-Government standards is considered less important than military documents. Another problem is that manufacturers on technical committees sometimes oppose the development of product standards since they might exclude their product, or level the playing field, making product differences that are now marketed as selling points less important.

There is also some question about the Department's commitment to using non-Government standards since there is usually considerable delay in adopting a standard. In part, this delay is the result of a complex, bureaucratic adoption process that could be simplified while still protecting the Department's interests. Usually, adoption is a fairly time-consuming process demanding a modest amount of resources. When a defense activity determines that a non-Government standard is suitable for adoption, a one-page adoption notice is prepared, coordinated for 60 to 90 days, differing comments are resolved, and finally, the document may be adopted. The whole process can take anywhere from 3 months to a year, and when the originating non-Government standards body revises the document, the revised document must be adopted again using the same procedures.

This cumbersome process causes delays in adoption and, in some cases, discourages adoption. Because of time lags to readopt revised documents, it is common for a standard listed as adopted by the Department of Defense not to be the most current issue. To encourage the rapid adoption of the most current issue of a non-Government standard, we propose to eliminate the formal adoption notice and coordination. Instead, a standardization management activity would act as a proponent to determine the adequacy of a non-Government standard for use within the Department of Defense. The proponent would be encouraged to circulate the draft standard throughout the Department as part of the normal coordination process for that non-Government standards body, but no coordination would occur after approval of the standard. Instead of an adoption notice, the proponent's name and address would appear on the first page of the standard as the focal point for the Department of Defense, and the standard would be indexed in the *Department of Defense Index of Specifications and Standards*. Once adopted by the Department, all future updates to a non-Government standard would automatically be adopted. Acceptance of a non-Government standard would be perpetual, unless a withdrawal of interest notice were issued by the proponent.

Recommendations

The adoption process will be simplified to encourage the use of non-Government standards and lessen the administrative burden on the standardization management activities by eliminating the need for formal coordination and for the readoption of future revisions to a non-Government standard.

The Departmental Standardization Offices and standardization executives will be responsible for ensuring consistent Department of Defense participation on non-Government standards committees.

"The adoption process will be simplified to encourage the use of non-Government standards. . ."

Automation

Conclusion

Automation is the key to improving the development, storage, retrieval, dissemination, application, and analysis of specifications, standards, and other standardization documents. Without automation, managers and users will not have meaningful information provided on a timely basis.

Discussion

The standardization world has been slow to take advantage of automation to improve document productivity and usefulness. The newly operational Print On Demand System is a major step forward in the storage, retrieval, and dissemination of specifications and standards, but much remains to be done. A Standardization Automation Users Panel met for the first time in July 1988 to explore various ways to improve standardization through automation and to select an administrator to manage the future data bases. A study team is visiting various isolated islands of automation that support standardization on a limited basis to determine if their applications could be expanded and made available throughout the Department of Defense.

Recommendations

The Standardization Automation Users Panel will develop a plan to automate the various functional requirements of the Defense Standardization Program. As a minimum, the Panel will consider the following for automation: the *Department of Defense Index of Specifications and Standards*, the standardization directory, the status of standardization projects, automatic coordination, document transmission to the Department of Defense Single Stock Point, key word searches, full text access, a specifications and standards tiering data base, and a standardization bulletin board. The Standardization Automation Users Panel will also work closely with the Computer Aided Acquisition and Logistics Support office to ensure compatibility with their efforts, and to develop an interface with industry that reduces duplicative generation and maintenance of data, thus eliminating the requirements for expensive paper output and reentry of data.

"The Standardization Automation Users Panel will develop a plan to automate the various functional requirements of the Defense Standardization Program."

The Standardization Automation Users Panel will consider alternatives to the Department of Defense Single Stock Point as the administrator for these data bases, and assess both location and control of future automated data bases.

Training

Conclusion

Widespread and properly tailored training is essential if the Department of Defense is to refrain from issuing excessive military specifications, and consider developing and using alternatives, such as non-Government standards and multiple award schedules. Training is also needed to improve the effectiveness of the management of the Defense Standardization Program.

Discussion

There is not enough training available to satisfy the needs of specifications and standards developers and users. The primary course available is the Defense Specification Management Course taught by the Army Logistics Management College, which can only accept a limited number of students and concentrates primarily on the needs of the specification writer to develop and manage military specifications. Courses are needed to address alternatives to military specifications and standards. Specialized training modules should be developed to address the peculiar needs of the users of standardization documents, such as those involved in logistics, quality assurance, packaging, engineering, and library science. Personnel must be better trained to carry out their management responsibilities as a lead standardization activity. With its many training sites and capabilities, the Defense Systems Management College would be a likely candidate to assign the development of these new courses.

Recommendations

The Defense Systems Management College will be assigned the task to develop training courses that are better suited for targeted audiences, that more closely reflect current policies on document development and preference for use, and that address management responsibilities within the Defense Standardization Program. The Army Logistics Management College will modify its existing specification course to place less emphasis on the development of military specifications, and more emphasis on such alternatives as non-Government standards, commercial item descriptions, and multiple award schedules.

"The Defense Systems Management College will be assigned the task to develop training courses. . ."

"The Army Logistics Management College will modify its existing specification course. . ."

Funding

Conclusion

An executive agent needs to be designated to program and budget funds to be used by the Military Departments and Agencies to accomplish special standardization projects.

Discussion

In general, standardization management activities are funded from operations and maintenance funds to accomplish certain command objectives, or they are funded from other sources to complete a specific task. While certain projects are well served by this funding method, broad corporate objectives serving the Department of Defense as a whole frequently are not. Examples of corporate standardization activities that could be enhanced by additional centralized funding include the development of metric standards to ensure greater interoperability with our allies, joint projects with non-Government standards bodies to develop world class standards, and automation. In order to make standardization management activities more responsive to corporate defense standardization objectives, a single Military Department or Agency needs to be assigned as the executive agent and directed to program and budget money for corporate standardization activities.

"Designate a single Military Department or Agency to program and budget funds as the executive agent for Defense Standardization Program special projects."

Recommendation

Designate a single Military Department or Agency to program and budget funds as the executive agent for Defense Standardization Program special projects.

Forging the Right Relations With Industry

Conclusion

By improving the interface between the standardization management activities and industry associations and non-Government standards bodies, the Department of Defense can forge the right relationships with industry and take advantage of their resources to improve our specifications and standards.

Discussion

While relations between standardization management activities and industry are good, they can be improved. One great source of frustration for industry is simply not knowing who to contact in the Department of Defense when problems, opportunities, and questions arise involving various commodities or documents. Non-Government standards committees also experience similar problems when they seek defense participation to develop standards. What is needed is an easy to use directory identifying the key players in the Department, together with their phone numbers, addresses, commodity areas, and any non-Government standards bodies or industry associations in which they participate.

To be successful in improving the existing specifications and standards, the Department of Defense needs to take advantage of the potential services that could be provided by industry associations and non-Government standards bodies. These organizations could be used to conduct surveys, create small working groups to address specific issues, and get a better pulse on whether problems we hear about affect an entire industry or just a company within that industry. There should also be regularly scheduled meetings with the major multi-industry associations to address policy issues and problems with defense acquisition documents. This would foster better relations, solve some persistent problems, and give industry a better understanding of defense needs.

Recommendations

The Director, Standardization and Data Management will establish regular meetings with the major industry associations to identify and solve problems with specifications and standards used by the Department of Defense. Industry associations will be used to conduct surveys of their members, and create special task groups to solve specific issues. A standardization directory will be prepared to help industry and non-Government standards bodies identify the proper people to serve on technical committees and address standardization problems and opportunities.

"A standardization directory will be prepared. . ."

Feedback on Specifications and Standards

Conclusion

To identify more effectively those specifications and standards containing redundant, conflicting, technically obsolete, and restrictive requirements, there must be more feedback from the users of these documents.

Discussion

Nearly all military specifications and standards give the address of the preparing activity for the document, and encourage comments either by letter or via the Standardization Document Improvement Proposal Form that is attached to the back of the document. Despite this encouragement, the number of comments received annually tends to be small. There are several reasons for such meager feedback. Some users either do not have the time or incliation to fill out a form or write a letter. Others complain they never receive a response to their comments, or that the response avoids consideration of the comment until the next time the document is updated. More feedback might be received if the telephone number of the preparing activity was included on the Standardization Document Improvement Proposal Form. To ensure the correct preparing activity receives the comment and provides an adequate response in a timely manner, a central control point to process the forms could be established.

Recommendations

"The Standardization Document Improvement Proposal Form will be revised. . ."

The Standardization Document Improvement Proposal Form will be revised to include the telephone number of the preparer and a self-addressed focal point that will be responsible for ensuring a timely and adequate response.

Reporting Standardization Accomplishments

Conclusion

The image of specifications and standards could be enhanced by improving the quality of the annual Standardization Accomplishment Report. The report could also serve as a gauge to measure the effectiveness of the Military Departments and Agencies in meeting policy goals and objectives.

Discussion

The primary reporting mechanism for standardization accomplishments is the annual Standardization Accomplishment Report, which could be a useful tool to measure our progress towards certain goals. Past reports provided statistics on numbers of documents developed, updated, and canceled; there was some required information on avionics standardization and the parts control program; and the Military Departments/Agencies would report on accomplishments from their individual activities. To a large extent, the report rambled, lacked focus, and the accomplishments seldom reflected those of the entire Military Department or Agency.

The annual Standardization Accomplishment Report should be revitalized to measure our progress. Each year, the Office of the Secretary of Defense should work with the Military Departments and Agencies to establish goals against which progress will be reported. The annual report should also contain general statistical data and the top five significant accomplishments for the entire Military Department or Agency.

Recommendation

The format and required information from the Military Departments and Agencies for the fiscal year 1989 Standardization Accomplishment Report will be changed to provide more concise and meaningful data. This change will be incorporated into the *Defense Standardization Manual.*

". . .the fiscal year 1989 Standardization Accomplishment Report will be changed to provide more concise and meaningful data."

Department of Defense Index of Specifications and Standards

Conclusion

Misconceptions about military specifications and standards are often the result of misunderstanding the format and content of the *Department of Defense Index of Specifications and Standards.*

Discussion

Many people who examine the *Department of Defense Index of Specifications and Standards* conclude incorrectly that all the documents listed are specifications and standards prepared by and for the Department of Defense. Based on the title of the *Index*, this conclusion is logical, but in fact, there are thousands of documents listed that are not specifications or standards, and there are thousands of documents prepared by either non-Government standards bodies or the General Services Administration.

To correct this misconception, the *Index* should be changed to the *Federal Index of Specifications and Standards*, and divided into three volumes: a listing of federal documents, such as federal specifications and standards, commercial item descriptions, and federal information processing standards; a listing of uniquely military documents; and a listing of adopted non-Government standards. Although the Department of Defense Single Stock Point could maintain such an *Index*, it might be more appropriate to examine if the National Institute of Standards and Technology would be willing to accept this responsibility.

Within the proposed listing of uniquely military documents, military specifications should be segregated into reprocurement and development documents. The Department is sometimes criticized for specifications that give explicit design detail. Such criticism is valid in the case of development, and it may be valid for reprocurement, but we need to acknowledge there are reprocurement situations where it is necessary to provide explicit design specifications.

Another problem with the *Department of Defense Index of Specifications and Standards* is the large number of errors in it. It will be a laborious undertaking to verify the accuracy of the *Index*, but given its legal importance in contractual matters, it is a necessary task.

"The Department of Defense Index of Specifications and Standards will be reformatted . . . and the National Institute of Standards and Technology will be asked to maintain the reformatted Index."

Recommendations

The *Department of Defense Index of Specifications and Standards* will be reformatted to convey better the types of documents used in the Defense Standardization Program. The Military departments and Agencies will review the *Index* for accuracy and make the necessary corrections, and the National Institute of Standards and Technology will be asked to maintain the reformatted *Index*.

Lead Standardization Activity Responsibilities

Conclusion

The lead standardization activities are not adequately fulfilling their functions in the way they manage federal supply classes and standardization areas.

Discussion

A lead standardization activity is responsible for managing the standardization documents under a specific federal supply class or standardization area (see Appendix A for a listing of lead standardization activities). In this role, a lead standardization activity assigns project numbers authorizing the development, update, adoption, and cancellation of standardization documents to prevent duplicative efforts and ensure adherence to policy. It is also responsible for developing and monitoring program plans to identify standardization problems and opportunities, to prioritize standardization efforts, and to assign tasks within the Military Departments and Agencies.

While the *Defense Standardization Manual* establishes the lead standardization activity's responsibilities and authorities, there is much inconsistency in the way they translate their responsibilities into practice. Some lead standardization activities challenge requests to develop or change a standardization document; but most routinely approve the requests. Some use the program plan as a blueprint for the future; but others either ignore their responsibility or issue meaningless plans that fulfill the letter, but not the spirit of the requirement. Part of the problem might be that the lead standardization activities were identified over 30 years ago, and at least in some cases, they may no longer have the dominant technical capability or interest to enable them to do a good job. There should be a review of all the lead standardization activity assignments to ensure that each federal supply class and standardization area is managed by the proper activity. Consideration should also be given to designating a civilian agency as a lead standardization activity. For example, the General Services Administration has the Government's technical expertise for hand tools and prepares the vast majority of hand tool specifications and standards used by the Department of Defense. If they agree, the General Services Administration would seem the logical lead standardization activity for the hand tools federal supply classes.

Recommendations

The current lead standardization activity assignments will be reevaluated for appropriateness, and reassigned as necessary. In addition, the lead standardization activity will be required to complete a project questionnaire before authorizing the development or update of any specification or standard to ensure the need for the document and compliance with standardization policies. Such a questionnaire will document management decisions, and will provide a permanent record to audit these decisions.

"The current lead standardization activity assignments will be reevaluated for appropriateness, and reassigned as necessary."

MIL-C-1029E
28 September 1973

SUPERSEDING
MIL-C-001029D(GL)
31 December 1970, and
MIL-C-1043D
27 March 1968, and
MIL-C-1029C
15 September 1966

MILITARY SPECIFICATION

COOKIES, OATMEAL WITH CHOCOLATE CHIPS AND SANDWICH: CANNED

This specification is approved for use by all Departments and Agencies of the Department of Defense.

1. SCOPE

1.1 Scope. This specification covers canned cookies, oatmeal with chocolate chips, and cookies, sandwich, which are used as a dessert component in operational rations.

1.2 Classification. The cookies shall be of the following types and styles, as specified (see 6.1):

Type I - Oatmeal with chocolate chip

Type II - Sandwich

Style A - Vanilla-flavored filling

Style B - Chocolate-flavored filling

* 2. APPLICABLE DOCUMENTS

2.1 The following documents, of the issues in effect on date of invitation for bids or request for proposal, form a part of this specification to the extent specified herein:

SPECIFICATIONS

FEDERAL

C-M-350 - Milk Nonfat, Dry
N-C-195 - Cereal, Rolled Oats

FSC 8920

THIS DOCUMENT CONTAINS 15 PAGES.

(Technical society and technical association specifications and standards are generally available for reference from libraries. They are also distributed among technical groups and using Federal agencies.)

3. REQUIREMENTS

3.1 Materials. All materials shall be clean, sound, wholesome, and free from evidence of insect infestation or other objectionable foreign matter.

3.1.1 Flour, enriched. The flour shall be wheat flour, bleached or unbleached, and shall be matured. The flour shall be enriched in accordance with the Definitions and Standards of Identity for Enriched flour under the Federal Food, Drug and Cosmetic Act and regulations promulgated thereunder.

3.1.2 Sugar. Sugar shall be white refined cane or beet sugar or a combination thereof, either powdered or granulated, as required for the specific product.

3.1.3 Shortening. The shortening shall be refined vegetable oil and shall have a stability of not less than 100 hours as determined by the active oxygen method (AOM).

3.1.4 Rolled oats. Rolled oats shall conform to quality requirements for type I of N-C-195.

3.1.5 Salt. Salt shall be white, refined, sodium chloride with or without anticaking agent. Iodized salt shall not be used.

3.1.6 Egg products. The egg product shall be fresh whole eggs, frozen whole eggs, dried whole eggs, or a combination thereof in the proper proportion so as to comply with the formulation requirements of 3.2. All egg products shall have been produced and handled in compliance with requirements set forth in the USDA publication entitled "Regulations Governing he Grading and Inspection of Egg Products". They shall be prepared under con~~inuous inspection of the USDA and shall bear the inspection shield mark.~~ gg products shall have been tested and certified Salmonella negative by the ~~USDA.~~

3.1.7 Milk, dry, nonfat. Nonfat dry milk shall be extra grade of high heat ype and shall be spray processed (conventional), as specified in C-M-350.

3.1.8 Leavening agents. Leavening agents shall be sodium bicarbonate, mmonium bicarbonate and monocalcium phosphate or other appropriate leavening gents. The leavening agents shall conform to Food Chemical Codex.

3.1.9 Vanilla flavoring. Vanilla flavoring shall be pure vanilla bean extract, vanillin or ethyl vanillin or a combination thereof.

3.1.10 Chocolate chips. Chocolate chips shall be made from semisweet chocolate which meets the requirements in the Definitions and Standards for Chocolate and Cocoa Products under the Federal Food, Drug and Cosmetic Act. The chocolate chips shall be in the form of chips or drops. The fat content shall be not less than 28.0 percent. The count per pound shall be not less than 3000 nor more than 4400.

* 3.1.11 Cocoa. Cocoa shall conform to the product requirements of medium fat cocoa as defined in JJJ-C-501.

* 3.1.12 Plastic fat. The plastic fat used in the filling shall conform to 3.1.3 except that hydrogenated cocunut oil may be used. In addition, when hydrogenated coconut oil is used the melting point shall be within the range of 100°F. to 110°F. It shall have a plasticity suitable for the production of sandwich cookie filling. It may contain added lecithin or other suitable plasticizing agents.

3.1.13 Vitamins. Ascorbic acid (vitamin C) and thiamine hydrochloride shall comply with Food Chemical Codex.

3.2 Formulas (types I and II cookies).

3.2.1 Type I. Oatmeal cookies with chocolate chips shall be prepared from the following ingredients in the proportions indicated:

TABLE I. Oatmeal cookies, chocolate chips

Material	Parts by weight
Flour	not more than 100
Sugar	not more than 105
Nonfat dry milk	not less than 6
Eggs (on a liquid basis)	not less than 20
Shortening	not less than 65
Rolled oats	not less than 45
Chocolate chips	not less than 62.5
Salt	not less than 1.5 or more than 1.20
Bicarbonate of soda	(as required)
Flavoring	(as required)
Water	(variable)

3.2.2 Type II. Sandwich, cookie, styles A and B, shall be prepared from the following ingredients in the proportions indicated:

TABLE II. Base cake (sandwich)

Material	Parts by weight
Flour	not more than 100
Sugar	not more than 35
Shortening	Not less than 25
Salt	not less than 1.10 or more than 1.25
Baking soda	(as required)
Ammonium bicarbonate	(as required)
Monocalcium phosphate	(as required)
Water	(as required)

TABLE III. Filling formula (vanilla)

Material	Parts by weight
Powdered sugar	not more than 100
Plastic fat	not less than 50 nor more than 60 1/
Vanilla	(as required)

1/ Exact amount between specified limits to be adjusted to yield proper consistency for stenciling.

TABLE IV. Filling formula (chocolate)

Material	Parts by weight
Powdered sugar	not more than 100
Plastic fat	not less than 50 nor more than 60 1/
Cocoa	not less than 10
Vanilla	(as required)

1/ See footnote 1/ of table III.

3.2.3 Vitamin content in fillings. The cookie fillings, styles A and B, shall be fortified with vitamins and shall contain the following minimum vitamin levels:

Thiamine hydrochloride (Vitamin B-1) - Not less than 0.8 milligrams per 14.18 grams of filling.

Ascorbic acid (Vitamin C) - Not less than 37.5 milligrams per 14.18 grams of filling.

3.3 Finished product.

3.3.1 Type I, oatmeal with chocolate chips. The cookies shall be well-baked. They shall be browned on the bottom surface and outer edges, but not appreciably browned on the top surface. They shall be wholly intact, free of checks or cracks. The weight of each cookie shall be not less than 13.7 grams. The diameter of each cookie at its greatest dimension shall be such as to enable easy placement of the cookie in the required lined can. However, the diameter at its greatest dimension shall be not less than 2-5/16 inches. The cookies shall be tender and crisp with an appetizing flavor, free of a burnt or scorched flavor. Moisture content shall be not greater than 5.0 percent.

3.3.2 Type II, sandwich. Each cookie shall consist of two round base cakes with a layer of filling between them. The weight of a cookie shall be not less than 21.5 grams with the filling weighing not less than 6.4 grams. The base cakes shall have been uniformly well-baked with a color ranging from-not lighter than chip 27885 or darker than chip 13711 of FED-STD-595 for colors. The color comparisons shall be made under north sky daylight with the objects held in such a way as to avoid specular refractance (glossiness). The moisture content of the base cakes shall be not greater than 5.0 percent by weight. The filling shall be centered so that it does not protrude beyond the perimeter of the base cakes. The filling shall be fortified as specified in 3.2.3. The cookie shall be wholly intact, free of checks or cracks. The diameter of the cookie shall be such that the cookie can easily be placed in the required lined can. However, the diameter shall be not less than 2-6/16 inches. The cookie shall be tender and crisp and have an appetizing flavor, free of a burnt or scorched flavor.

3.3.3 Height of cookies. The cookies shall have an overall height which will preclude damage to them when packaged as specified in 5.1. The minimum height of the cookies in the can shall be 1-1/2 inches.

3.4 Federal Food, Drug, and Cosmetic Act. All deliveries shall conform in every respect to the provisions of the Federal Food, Drug, and Cosmetic Act and regulations promulgated thereunder.

3.5 Workmanship. The product shall be processed in establishments meeting the requirements of MIL-STD-1105. It shall be prepared and processed with minimum delay between the various stages in production.

4. QUALITY ASSURANCE PROVISIONS

4.1 Responsibility for inspection. Unless otherwise specified in the contract or purchase order, the supplier is responsible for the performance of all inspection requirements as specified herein. Except as otherwise specified in the contract or order, the supplier may use his own or any other facilities suitable for the performance of the inspection requirements specified herein, unless disapproved by the Government. The Government reserves the right to perform any of the inspections set forth in the specification where such inspections are deemed necessary to assure supplies and services conform to prescribed requirements.

4.2 Preacceptance inspection (plant sanitation inspection). The product shall be rejected if produced in plants not meeting the requirements of 3.5.

4.3 Inspection. Sampling for inspection shall be performed in accordance with MIL-STD-105, except where otherwise indicated hereinafter.

4.3.1 Component and material inspection. In accordance with 4.1, components and materials shall be inspected in accordance with all the requirements of referenced specifications, drawings and standards unless otherwise excluded, amended, modified or qualified in this specification or applicable purchase documents.

4.3.1.1 Examinations.

4.3.1.1.1 Identity. Conformance of ingredients to identity (kind, count of chocolate chips, Chemical Codex quality, grade, U.S.D.A inspection and certification - as applicable) shall be ascertained by examination of pertinent labels, invoices and other valid documents, presence of U.S.D.A shield on egg products containers and certification for Salmonella negative egg product.

* 4.3.1.1.2 Condition. Each ingredient, except rolled oats, shall be examined organoleptically, as necessary, to determine conformance to 3.1. When examining shortening and plastic fat, odor and taste determinations shall be performed by heating the item to 350°F checking for off odors and then cooling item to approximately 100°F and checking for off flavors. The sample unit for examination shall be approximately 1 pound of ingredient (1 ounce for vitamins and vanilla flavoring) derived from each of 5 primary containers. In the event a lot consists of less than five containers, a sample unit shall be extracted from each container in the lot. One or more sample units not conforming to condition requirements shall indicate an unacceptable ingredient and use of such shall be cause for rejection of the involved finished product.

MIL-H-22547B(YD)
16 July 1976
SUPERSEDING
MIL-H-22547A(YD)
6 February 1973

MILITARY SPECIFICATION

HEAT PUMPS, HEATING AND COOLING (UNITARY) (8,400 to 300,000 BTU)

This specification is approved for use by the Naval Facilities Engineering Command, Department of the Navy, and is available for use by all Departments and Agencies of the Department of Defense.

1. SCOPE

1.1 Scope. This specification covers air-to-air, and water-to-air heat pumps designed to perform the functions of both heating and cooling with controlled temperature, circulating, filtering, cleaning, and dehumidifying of an air stream. The heating functions may be supplemented by electric resistance heaters.

1.2 Classification. The heat pump shall be of the following types, classes, and sizes as specified (see 6.2.1).

Type I - Heat pump, factory assembled refrigerant circuit or circuits (packaged unit).
Type II - Heat pump (split-system) employing remote outdoor section from indoor section.

Class A - Air-to-air.
Class B - Water-to-air.

Size 1 - 8,400 - 84,000 British thermal units per hour (Btu/hr).
Size 2 - 85,000 - 300,000 Btu/hr.

2. APPLICABLE DOCUMENTS

2.1 Issues of documents. The following documents, of the issue in effect on date of invitation for bids or request for proposal form a part of this specification to the extent specified herein.

Beneficial comments (recommendations, additions, deletions) and any pertinent data which may be of use in improving this document should be addressed to: Commanding Officer (156), Naval Construction Battalion Center, Port Hueneme, CA 93043 by using the self-addressed Standardization Document Improvement Proposal (DD Form 1426) appearing at the end of this document or by by letter.

FSC 4120

STANDARDIZATION DOCUMENT IMPROVEMENT PROPOSAL	OMB Approval No. 22-R255

INSTRUCTIONS: The purpose of this form is to solicit beneficial comments which will help achieve procurement of suitable products at reasonable cost and minimum delay, or will otherwise enhance use of the document. DoD contractors, government activities, or manufacturers/vendors who are prospective suppliers of the product are invited to submit comments to the government. Fold on lines on reverse side, staple in corner, and send to preparing activity. Comments submitted on this form do not constitute or imply authorization to waive any portion of the referenced document(s) or to amend contractual requirements. Attach any pertinent data which may be of use in improving this document. If there are additional papers, attach to form and place both in an envelope addressed to preparing activity.

4120-N223

DOCUMENT IDENTIFIER AND TITLE
MIL-H-22547B(YD) - HEAT PUMPS, HEATING AND COOLING (UNITARY) (8,400 TO 300,000 BTU)

NAME OF ORGANIZATION AND ADDRESS

CONTRACT NUMBER

MATERIAL PROCURED UNDER A
☐ DIRECT GOVERNMENT CONTRACT ☐ SUBCONTRACT

1. HAS ANY PART OF THE DOCUMENT CREATED PROBLEMS OR REQUIRED INTERPRETATION IN PROCUREMENT USE?

A. GIVE PARAGRAPH NUMBER AND WORDING.

B. RECOMMENDATIONS FOR CORRECTING THE DEFICIENCIES

2. COMMENTS ON ANY DOCUMENT REQUIREMENT CONSIDERED TOO RIGID

3. IS THE DOCUMENT RESTRICTIVE?

☐ YES ☐ NO *(If "Yes", in what way?)*

4. REMARKS

SUBMITTED BY *(Printed or typed name and address - Optional)*

TELEPHONE NO.

DATE

DD FORM 1 JAN 72 1426 REPLACES EDITION OF 1 JAN 66 WHICH MAY BE USED S/N 0102-014-1802

☆U.S. GOVERNMENT PRINTING OFFICE: 1973—714-666/3903 2-1

NOTE: This draft, dated 02 August 1988, prepared by the Naval Facilities Engineering Command, Naval Construction Battalion Center, Port Hueneme, CA, has not been approved and is subject to modification. DO NOT USE FOR ACQUISITION PURPOSES. (Project No. 4120-N316)

| INCH-POUND |

MIL-H-22547B(YD)

SUPERSEDING
MIL-H-22547A(YD)
16 July 1976

PROPOSED MILITARY SPECIFICATION

HEAT PUMPS, HEATING AND COOLING (UNITARY) (8,400 TO 300,000 BTU)

(Preamble to be added)

1. SCOPE

1.1 Scope. This specification covers air-to-air, and water-to-air heat pumps designed to perform the functions of both heating and cooling with controlled temperature, circulating, filtering, cleaning, and dehumidifying of an air stream. The heating functions may be supplemented by electric resistance heaters.

1.2 Classification. The heat pump shall be of the following types, classes, and sizes as specified (see 6.2).

Type I - Heat pump, factory assembled refrigerant circuit or circuits (packaged unit).
Type II - Heat pump (split-system) employing remote outdoor section from indoor section.

Class A - Air-to-air.
Class B - Water-to-air.

Size 1 - 8,400 - 84,000 British thermal units per hour (Btu/hr).
Size 2 - 85,000 - 300,000 BTU/hr.

1.2.1 Part numbers. The specification number, type, combined to form the specification part numbers for the heat pumps covered by this specification (see 6.5). The part numbers for the Heat Pump Units are established as follows:

```
                                    M22547 - X - X - X
                                         |     |   |   |
Specification number--------------------     |   |   |
Type code number (see 6.5)-------------------    |   |
Class code number (see 6.5)-----------------------   |
Size code number (see 6.5)----------------------------
```

(Standardization Document Improvement Proposal to be added)

| FSC 4120 |

TABLE VII. Code number to class

Class 1 - 1
Class 2 - 2

6.5.4 Sizes. The sizes of the Heat Pumps (see 1.2) are identified by a one-digit number (see Table VIII).

TABLE VIII. Code number size

Size 1 - 1
Size 2 - 2

6.6 Subject term (keyword) listing.

Cooling
Heating
Pumps
Unitary

6.7 Changes from previous issue. Asterisks are not used in this revision to identify changes with respect to the previous issue due to the extensiveness of the changes.

Preparing activity

Navy - YD

(Project No. 4120-N316)

C. CONTRACT CLAUSES

SUBCOMMITTEE ON OVERSIGHT OF GOVERNMENT MANAGEMENT STAFF REVIEW OF CLAUSES IN DOD CONTRACTS FOR COMMERCIAL PRODUCTS

A. Actual Oscilloscope Solicitations

The Subcommittee staff reviewed the contract clauses included in six separate DOD solicitations for the commercial purchase of oscilloscopes -- an instrument for measuring variations in electrical current. The staff found that 171 different contract provisions were included in at least one of the six solicitations. Of these contract clauses, only 27 were included in all six of the solicitations; an additional 14 were included in five of the solicitations; 16 were included in four of the solicitations; 37 were included in three of the solicitations; 37 were included in two of the solicitations; and 40 were unique to one of the solicitations.

These numbers include only standard clauses from the Federal Acquisition Regulation and the Defense supplement to the FAR. They do not include: (a) clauses relating only to ths submission of bids and proposals; or (b) "local clauses" imposed by individual commands.

B. Hypothetical Oscilloscope Contracts

The Subcommittee staff asked one contracting officer from each of the three services to prepare a model commercial contract for oscilloscopes, using normal procedures. Each contracting officer was told that: (a) the contract was for commercial, off-the-shelf oscilloscopes; (b) the contract price was $750,000; (c) there was full and open competition; and (d) the contract was firm, fixed price, with the award based on adequate price competition.

The Air Force version of the contract included 107 standard clauses, the Navy version 85 contract clauses, and the Army version 99 contract clauses, with a total of 140 different standard clauses included in at least one of the three versions. Only 58 clauses were included in all three of the contracts and 32 clauses were included in two out of three, while 51 clauses were unique to the contract prepared by one of the three services.

These numbers do not include: (a) clauses relating only to ths submission of bids and proposals; or (b) "local clauses" imposed by individual commands. The Air Force contracting officer imposed 29 local clauses; the Navy contracting officer imposed 33; and the Army contracting officer imposed 35, for a total of 97 local clauses in the three model contracts. Each of these 97 local clauses was unique to the service imposing the requirement.

SUBMITTED BY THE DEPARTMENT OF DEFENSE, JUNE 28, 1988

DISCUSSION OF CLAUSES THAT ALL SERVICES DID NOT INCLUDE

CLAUSE	TITLE	REF
52.203-2	**CERTIFICATE OF INDEPENDENT PRICE DETERMINATION**	3.103-1

- -- **Purpose:** To ensure that prices were not the result of collusion between contractors.
- -- **Applicability:** In solicitations over $25K when a FFP contract is contemplated (with 4 exceptions, none of which apply).
- -- AR and NV included; AF did not.
- -- ALL services should have included.

CLAUSE	TITLE	REF
252.203-7002	**STATUTORY COMPENSATION PROHIBITIONS AND REPORTING REQUIREMENTS RELATING TO CERTAIN FORMER DEPARTMENT OF DEFENSE (DOD) EMPLOYEES**	203.170-5

- -- **Purpose:** To ensure former DoD officials who performed procurement-related functions in connection with a major defense contractor do not receive compensation from that same contractor for a period of two years after such officials have left service with DoD.
- -- **Applicability:** All contracts in excess of $100K.
- -- AF and AR included; NV did not.
- -- ALL services should have included.

CLAUSE	TITLE	REF
52.204-1	**APPROVAL OF CONTRACT**	4.103

- -- **Purpose:** To state the contract is subject to the written approval of the designated agency official.
- -- **Applicability:** In solicitations and contracts over $25K if required by agency procedures.
- -- AF included; AR and NV did not.
- -- FAR allows flexibility between agencies.

252.204-7007 COMMERCIAL AND GOVERNMENT ENTITY (CAGE) CODE REPORTING 204.670-3(B)(1)

- -- **Purpose:** To obtain code to be used for DD 350 reporting to identify commercial and government activities.
- -- **Applicability:** All contracts over $25K.
- -- AR and NV included; AF did not.
- -- Although it is necessary to obtain CAGE code for all contractors, AF may have obtained code from other sources (published info; on-line access to CAGE files; DD 2051 submitted by contractor to obtain code; prior contract).

252.205-7000 RELEASE OF INFORMATION TO COOPERATIVE AGREEMENT HOLDERS 205.470(c)

- -- **Purpose:** To obtain agreement from Defense contractors to provide (when requested) to cooperative agreement holders, a list of employees or offices responsible for entering into subcontracts. A "cooperative agreement holder" is one who has an agreement with DLA to furnish procurement technical assistance to business entities.
- -- **Applicability:** All solicitations and contracts when the contract amount is expected to exceed $500K.
- -- AF and AR included; NV did not.
- -- ALL services should have included.

52.207-4 ECONOMIC PURCHASE QUANTITY -- SUPPLIES 7.203

- -- **Purpose:** To obtain information to furnish to appropriate inventory management/requirements development activities to facilitate the establishment and evaluation of economic order quantities.
- -- **Applicability:** All solicitations over $25K for supplies.
- -- AF and NV included; AR did not.
- -- Although information is required, the KO has the authority to determine (1) the Government already has the data, (2) the data is otherwise readily available, or (3) it is impracticable for the Government to vary its future requirements.

52.208-1 **REQUIRED SOURCES FOR JEWEL BEARINGS AND RELATED ITEMS** **8.203-1**

-- **Purpose:** To advise contractor that jewel bearings shall be acquired from the GOCO plant in North Dakota, and that related items shall be acquired either from domestic manufacturers or from the GOCO plant.

-- **Applicability:** In all solicitations and contracts over $25K in specified FSC (oscilloscopes are in FSC 6625 which is included).

-- AF included; AR and NV did not.

-- Clause is not required if KO knows item does not contain jewel bearings or related items; or if item is purchased and used outside the U.S., its possessions, and Puerto Rico.

52.208-2 **JEWEL BEARINGS AND RELATED ITEMS CERTIFICATE** **8.203-1(c)**

-- **Purpose:** To obtain contractor's certification regarding information relative to jewel bearings or related items.

-- **Applicability:** Solicitations that contain above clause 52.208-1.

-- AF and NV included; AR did not.

-- NV application is inconsistent, both clauses should have been in or not.

252.208-7003 **REQUIRED SOURCES FOR HIGH CARBON FERROCHROME (HCF)** **208.7603(a)**

-- **Purpose:** To ensure HCF is acquired from U.S. sources only.

-- **Applicability:** All contracts over $25K. One of several exceptions is if the item is standard commercial.

-- NV included; AF and AR did not.

-- Clause is not applicable.

252.208-7006 **REQUIRED SOURCES FOR ANTIFRICTION BEARINGS** 208.7905

-- **Purpose:** In view of the national security significance of bearings, DoD has determined that bearings should be of domestic manufacture to halt erosion of U.S. bearing industry which is important to meet industrial surge and mobilization requirements.

-- **Applicability:** All solicitations and contracts over $25K.

-- AR included; AF and NV did not.

-- Clause not required if (1) KO knows item does not contain bearings; or (2) purchasing foreign bearings for use overseas.

252.209-7001 **ACQUISITIONS FROM DEFENSE CONTRACTORS SUBJECT TO ON-SITE INSPECTION UNDER THE INTERMEDIATE-RANGE NUCLEAR FORCES (INF) TREATY** 209.103(S-71)

-- **Purpose:** To ensure contractors do not deny subcontract awards to defense contractors subject to on-site inspection under the INF Treaty solely or in part because of the presence of Soviet inspectors at the defense contractor's facility.

-- **Applicability:** All solicitations or contracts over $25K.

-- AF included; AR and NV did not.

-- ALL services should have included.

252.210-7000 **BRAND NAME OR EQUAL** 210.004(b)(3)(ii)(B)

-- **Purpose:** To provide prospective contractors with information relative to the "brand name or equal" purchase description.

-- **Applicability:** In solicitations where a brand name or equal purchase description is used.

-- AR used; AF and NV did not.

-- It is apparent that AR used a brand name or equal purchase description and the others used another type.

52.212-1 TIME OF DELIVERY - ALT I 12.104(a)(2)

-- **Purpose:** To advise contractor of the required delivery schedule.

-- **Applicability:** All solicitations and contracts must have the required delivery schedule set forth in one of several possible ways.

-- AF included; AR and NV did not.

-- Apparently, AF determined this was the delivery clause that best suited their needs. Since the AR and NV did not use a FAR or DFAR clause, it must be assumed that they used a "local" clause or other type of statement to set forth the delivery requirement.

52.212-7 NOTICE OF PRIORITY RATING FOR NATIONAL DEFENSE USE 12.304(a)

-- **Purpose:** To advise contractor that item is covered by the Defense Priorities and Allocations System (DPAS), a Department of Commerce regulation in support of authorized national defense programs.

-- **Applicability:** In all solicitations when the contract to be awarded will be a rated order.

-- AF and NV included; AR did not.

-- Apparently, the AF and NV identified the item as rated and the AR did not; however, the AR was inconsistent in the application of this clause and clause 52.212-8. Both clauses should be in or out.

52.212-9 VARIATION IN QUANTITY 12.403(a)

-- **Purpose:** To inform the contractor of any permissable variation allowed in the required quantity.

-- **Applicability:** In all solicitations and contracts when a fixed price supply contract is contemplated.

-- AF and AR included; NV did not.

-- ALL services should have included.

52.212-10 **DELIVERY OF EXCESS QUANTITIES OF $100 OR LESS** **12.403(b)**

- -- **Purpose:** To advise the contractor that (a) excess quantities of items totaling up to $100 in value may be retained without compensating the contractor; or (b) excess quantities of items totaling over $100 in value may, at the Government's option, be either returned at the contractor's expense or retained and paid for at the unit price.

- -- **Applicability:** Optional in solicitations and contracts when a fixed price supply contract is contemplated.

- -- AF and NV included; AR did not.

- -- Since the quantity of items was not a "given" in the hypotethical scenario, apparently AF and NV assumed the unit price could have been less than $100; however, the NV was inconsistent in their application by including this clause and clause 52.246-24, **LIMITATION OF LIABILITY - HIGH VALUE,** which is used if the unit cost exceeds $100K.

52.212-13 **STOP-WORK ORDER** **12.505(b)**

- -- **Purpose:** To provide coverage for situations that may occur during contract performance that cause the Government to order a suspension of work, or a work stoppage.

- -- **Applicability:** Optional for use in negotiated procurements for supplies.

- -- AF and NV included; AR did not.

- -- Apparently, AF and NV determined they required this protection and the AR did not.

52.212-15 **GOVERNMENT DELAY OF WORK** 12.505(d)

-- **Purpose:** Provides for the administrative settlement of contractor claims that arise from delays and interruptions in the contract work caused by the acts, or failures to act, of the KO.

-- **Applicability:** Required in solicitations and contracts when a fixed price contract is contemplated for supplies; use is optional when commercial or modified-commercial items are being acquired.

-- AF and NV included; AR did not.

-- Apparently, AF and NV determined they required this protection and the AR did not.

52.215-1 **EXAMINATION OF RECORDS BY COMPTROLLER GENERAL** 15.106-1(b)

-- **Purpose:** To advise contractor that the Comptroller General shall have access to and the right to examine any of the contractor's directly pertinent books, documents, papers, or other records involving transactions related to the contract, for 3 years after final payment.

-- **Applicability:** In all negotiated solicitations and contracts.

-- AF included; AR and NV did not.

-- If AR and NV used the sealed bidding method, the clause was not required; however, there is insufficient information to determine which method was used. If they used the negotiation method, the clause should have been included.

52.215-2 AUDIT - NEGOTIATION 15.106-2(b)

- -- **Purpose:** To advise contractor that the Government shall have access to and the right to examine any of the contractor's directly pertinent books, documents, papers, or other records involving transactions related to the contract, for 3 years after final payment.
- -- **Applicability:** In negotiated solicitations and contracts over $25K when contractor is required to submit cost or pricing data.
- -- AF included; AR and NV did not.
- -- Since solicitation was fully competitive and award was made on the basis of adequate price competition, cost or pricing data was not required; therefore, this clause is not applicable.

52.215-6 TYPE OF BUSINESS ORGANIZATION 15.407(c)(2)

- -- **Purpose:** To determine what type business entity the contractor is.
- -- **Applicability:** All solicitations.
- -- AF and NV included; AR did not.
- -- ALL services should have included.

52.215-11 AUTHORIZED NEGOTIATORS 15.407(c)(7)

- -- **Purpose:** For prospective contractors to identify the person(s) authorized to negotiate on behalf of the contractor on the particular solicitation.
- -- **Applicability:** All solicitations that will result in a negotiated contract.
- -- AF and NV included; AR did not.
- -- If AR used the sealed bidding method, the clause was not required; however, there is insufficient information to determine which method was used. If AR used the negotiation method, the clause should have been included.

52.215-20 **PLACE OF PERFORMANCE** **15.407(g)**

-- **Purpose:** For prospective contractors to identify the geographical location where the contract will be performed.

-- **Applicability:** All solicitations unless the Government specifies the place of performance.

-- AF and NV included; AR did not.

-- ALL services should have included.

52.215-23 **PRICE REDUCTION FOR DEFECTIVE COST OR PRICING DATA - MODIFICATIONS** **15.804-8(b)**

-- **Purpose:** Gives the Government the right to reduce the contract price if it was significantly increased because a subcontractor submitted defective data.

-- **Applicability:** When it is contemplated that cost or pricing data will be required for a modification regarding a price adjustment over $100K.

-- AF included; AR and NV did not.

-- Apparently, AF determined there was a possibility that cost or pricing data may be required if a modification was necessary.

52.215-25 **SUBCONTRACTOR COST OR PRICING DATA - MODIFICATIONS** **15.804-8(b)**

-- **Purpose:** Same as 52.215-23.

-- **Applicability:** Used in conjunction with 52.215-23.

-- AF included; AR and NV did not.

-- Apparently, AF determined there was a possibility that cost or pricing data may be required if a modification was necessary.

52.215-26 INTEGRITY OF UNIT PRICES 15.812-2

-- **Purpose:** To ensure that distribution of direct and indirect costs within contracts is on a basis that ensures that unit prices are in proportion to the item's base costs.

-- **Applicability:** All solicitations and contracts over $25K. Not required for commercial items sold in substantial quantities to the general public when the prices are, or are based on, established catalog or market prices.

-- AF included; AR and NV did not.

-- Although hypothetical parameters said item was "commercial, off-the-shelf", it was not stated that price was based on catalog or market price. Apparently, AF assumed they were not; AR and NV assumed they were.

52.215-33 ORDER OF PRECEDENCE 15.406-3(b)

-- **Purpose:** To resolve any possible inconsistencies in the solicitation or contract, clause sets forth the order of precedence of different sections.

-- **Applicability:** In all solicitations and contracts when using the negotiation method.

-- AF and NV included; AR did not.

-- If AR used the sealed bidding method, the clause was not required; however, there is insufficient information to determine which method was used. If they used the negotiation method, the clause should have been included.

52.215-34 EVALUATION OF OFFERS FOR MULTIPLE AWARDS 15.407(h)

-- **Purpose:** To advise prospective contractors of evaluations factors for award.

-- **Applicability:** In solicitations if the KO determines that multiple awards might be made if doing so is economically advantageous to the Government.

-- AF included; AR and NV did not.

-- Although there appears to be only one line item in this hypothetical solicitation, perhaps the AF anticipated a quantity split.

252.215-7000 **AGGREGATE PRICING ADJUSTMENT** **215.804-8(S-70)**

- -- **Purpose:** To define the term "aggregate price adjustment".
- -- **Applicability:** Used in conjunction with 52.215-23 and 52.215-25.
- -- AF included; AR and NV did not.
- -- Since AF determined clauses 52.215-23 and 52.215-25 were applicable, use of this clause is consistent.

252.217-7270 **IDENTIFICATION OF SOURCES OF SUPPLY** **217.7204(c)**

- -- **Purpose:** To obtain information from the contractor regarding the actual manufacturer, NSN and source of technical data for the purpose of enabling the KO to allow solicitation of all actual manufactuers of end items, parts, subassemblies and/or components, thereby allowing for enhancing competition and avoiding payment of additional costs where no significant value is added by dealers, distributors, and manufacturers other than the actual manufacturer.
- -- **Applicability:** All supply contracts except when the KO already has required information; the KO determines that it would not be practicable to require the contractor to provide the information (i.e., repetitive local purchases); or~~,~~ if the supplies are commercial items sold in substantial quantities to the general public if the contract provides for the acquisition of such supplies at catalog or market prices or if the contract is awarded through the use of full and open competition.
- -- AR included; AF and NV did not.
- -- Since contract was fully competitive and award was based on adequate price competition, the clause is not applicable. (AR application of this clause is inconsistent with clause 52.215-26, Integrity of Unit Prices.)

52.219-8 **UTILIZATION OF SMALL BUSINESS CONCERNS AND SMALL DISADVANTAGED BUSINESS CONCERNS** 19.708(a)

-- **Purpose:** To further the interests of small and small disadvantaged business.

-- **Applicability:** Solicitations and contracts when the contract amount is expected to be over $10,000 unless for personal services or if performance is not domestic.

-- AF and AR included; NV did not.

-- ALL services should have included.

252.219-7000 **SMALL BUSINESS AND SMALL DISADVANTAGED BUSINESS SUBCONTRACTING PLAN** 219.708(a)

-- **Purpose:** Same as clause 52.219-8.

-- **Applicability:** Used in conjunction with clause 52.219-8.

-- AF and AR included; NV did not.

-- ALL services should have included.

252.219-7007 **NOTICE OF EVALUATION PREFERENCE FOR SMALL DISADVANTAGED BUSINESS CONCERNS** 219.7002

-- **Purpose:** To give a perference to offers submitted by SDB firms.

-- **Applicability:** Used in conjunction with clause 252.219-7000. The evaluation preference does not apply in several instances, one of which is if the purchase is subject to the Trade Agreements Act and the contract price exceeds the threshold cited in 25.402.

-- AF included; AR and NV did not.

-- Clause should not have been included since purchase is subject to Trade Agreements Act.

252.219-7009 INCENTIVE PROGRAM FOR SUBCONTRACTING WITH SMALL AND SMALL DISADVANTAGED BUSINESS CONCERNS, HISTORICALLY BLACK COLLEGES AND UNIVERSITIES AND MINORITY INSTITUTIONS 219.708(c)(1)

-- **Purpose:** To further the interests of Small businesses, SDBs, HBCUs, and MIs.

-- **Applicability:** Used in conjunction with clause 52.219-9.

-- AF included; AR and NV did not.

-- Flexibility for KO to determine that inclusion of a monetary incentive is necessary to increase subcontracting opportunities for small businesses, SDBs, HBCUs, and MIs.

52.220-1 PREFERENCE FOR LABOR SURPLUS AREA CONCERNS 20.103(b)

-- **Purpose:** To further the interests of eligible labor area surplus area concerns and encourage contractors to place subcontracts with LSA concerns.

-- **Applicability:** In solicitations and contracts over $25K that are not set aside for LSA concerns.

-- AR and NV included; AF did not.

-- ALL services should have included.

52.220-4 LABOR SURPLUS AREA SUBCONTRACTING PROGRAM 20.302(b)

-- **Purpose:** To further the interests of eligible labor area surplus area concerns.

-- **Applicability:** Solicitations and contracts that (1) may exceed $500K, (2) contain clause 52.220-3, and (3) in the opinion of the KO, offer substantial subcontracting possibilities.

-- AF and NV included; AR did not.

-- Apparently, AF and NV determined substantial subcontracting opportunities exist; AR did not.

52.222-1 **NOTICE TO THE GOVERNMENT OF LABOR DISPUTES** 22.103-5(a)

-- **Purpose:** To require the contractor to notify the Government of labor disputes as they pertain to contract performance.

-- **Applicability:** In solicitations and contracts that involve programs or requirements that the HCA has determined it is necessary that contractors be required to notify the Government of actual or potential labor disputes that are delaying or threaten to delay the timely contract performance.

-- NV included; AF and AR did not.

-- Apparently, NV HCA determined it necessary, while AF and AR HCAs did not.

52.222-3 **CONVICT LABOR** 22.202

-- **Purpose:** To set forth policies and procedures controlling the employment of prison inmates in the performance of Government contracts.

-- **Applicability:** In solicitations and contracts when performance is to be domestic, unless the contract will be subject to the Walsh-Healey Public Contracts Act, which contains a separate prohibition against the employment of convict labor.

-- AR included; AF and NV did not.

-- Clause is applicable since requirement is not subject to the Walsh-Healey Public Contracts Act. (Walsh-Healey is covered by 41 USC 35 thru 45: 41 USC 35 states "all supplies"; however, 41 USC 45 states the Act does not apply to purchases of such materials, supplies, articles or equipment as may usually be bought in the open market.)

52.222-4 CONTRACT WORK HOURS AND SAFETY STANDARDS ACT - OVERTIME COMPENSATION 22.305(a)

-- **Purpose:** States no laborer or mechanic doing any part of the work contemplated by the contract shall be required or permitted to work more than 40 hours in any workweek unless paid for all such OT at not less than 1-1/2 times the basic rate of pay.

-- **Applicability:** In solicitations and contracts when the contract may require or involve the employment of laborers or mechanics. Use of clause is prohibited if contract is for supplies, materials, or articles ordinarily available in the open market.

-- NV included; AF and AR did not.

-- Clause is not applicable.

52.222-21 CERTIFICATION OF NONSEGREGATED FACILITIES 22.810(a)(1)

-- **Purpose:** To guarantee the personal rights of employees.

-- **Applicability:** In solicitations over $10K in conjunction with clause 52.222-26, Equal Opportunity.

-- NV included; AF and AR did not.

-- ALL services should have included.

52.222-22 PREVIOUS CONTRACTS AND COMPLIANCE REPORTS 22.810(a)(2)

-- **Purpose:** To obtain information from the contractor regarding his participation in previous contracts subject requirements of clause 52.222-26, Equal Opportunity, and to ensure he has filed all required reports.

-- **Applicability:** Used in conjunction with clause 52.222-26.

-- AR and NV included; AF did not.

-- ALL services should have included.

52.222-25 **AFFIRMATIVE ACTION COMPLIANCE** **22.810(d)**

- -- **Purpose:** To obtain information from the contractor regarding his affirmative action plan.
- -- **Applicability:** Used in conjunction with clause 52.222-26.
- -- AR and NV included; AF did not.
- -- ALL services should have included.

252.222-7000 **POTENTIAL APPLICATION OF THE SERVICE CONTRACT ACT, AS AMENDED (FIXED PRICE)** **222.1006(S-70)**

- -- **Purpose:** To set forth remedy of contractor in the event a contract originally represented as being subject to the Walsh-Healey Public Contracts Act is later changed to make the provisions of the Service Contract Act apply.
- -- **Applicability:** In solicitations and contracts for overhaul and modifications of equipment, which are considered by the KO to be subject to Walsh-Healey rather than the Service Contract Act.
- -- NV included; AF and AR did not.
- -- Clause is not applicable.

52.223-3 **HAZARDOUS MATERIAL IDENTIFICATION AND MATERIAL SAFETY DATA** **23.303**

- -- **Purpose:** Prescribes policies and procedures for acquiring deliverable items, other than ammunition and explosives, that require the furnishing of data involving hazardous materials.
- -- **Applicability:** In solicitations and contracts when it is contemplated that the contract will require the delivery of hazardous materials.
- -- NV included; AF and AR did not.
- -- Clause is not applicable.

52.223-5 **CERTIFICATION REGARDING A DRUG-FREE WORKPLACEE** 23.505

-- **Purpose:** To implement the Drug-Free Workplace Act of 1988.

-- **Applicability:** In solicitations of (1) any dollar value if the contract is expected to be awarded to an individual, or (2) $25K if contract is expected to be awarded to other than an individual.

-- AF and AR included; NV did not.

-- ALL services should have included.

252.223-7500 **DRUG-FREE WORK FORCE** 223.7504

-- **Purpose:** Prescribes policies and procedures concerning drug abuse as it impacts on the performance of defense contracts.

-- **Applicability:** In solicitations and contracts that involve access to classified information or any other contract when the KO determines that inclusion of the clause is necessary for reasons of national security or for the purpose of protecting the health or safety of those using or affected by the product of or the performance of the contract (except for commercial or commercial-type products).

-- NV included; AF and AR did not.

-- Clause is not applicable.

252.225-7000 **BUY AMERICAN-BALANCE OF PAYMENTS PROGRAM CERTIFICATE** 225.109(a)(S-70)

-- **Purpose:** For contractors to identify and certify whether end products are domestic or of foreign origin.

-- **Applicability:** Used with clause 252.225-7001, Buy American Act and the Balance of Payments Program.

-- AF and AR included; NV did not.

-- ALL services should have included.

252.225-7002 **QUALIFYING COUNTRY SOURCES AS SUBCONTRACTORS** **225.109(d)(S-72)**

-- **Purpose:** States no qualifying country source or U.S. source is to be precluded from competing for subcontracts.

-- **Applicability:** Used in conjunction with clauses 252.225-7001 or 252.225-7006.

-- AF and AR included; NV did not.

-- ALL services should have included.

252.225-7004 **IDENTIFICATION OF EXPENDITURES IN THE UNITIED STATES** **225.305(c)**

-- **Purpose:** To obtain information from contractors to facilitate reporting of amount of acquisitions of U.S. end products and services accomplished under the Balance of Payments Program

-- **Applicability:** Contracts exceeding $25K for supplies to be used outside the U.S.

-- NV included; AF and AR did not.

-- Apparently, NV assumed items were for use outside the U.S.; AF and AR did not.

252.225-7005 **BUY AMERICAN ACT - TRADE AGREEMENTS ACT - BALANCE OF PAYMENTS PROGRAM CERTIFICATE** **225.407(a)(1)**

-- **Purpose:** For contractors to identify and certify whether end products are domestic or of foreign origin.

-- **Applicability:** Used with clause 252.225-7006, Buy American Act, Trade Agreements Act, and the Balance of Payments Program.

-- NV included; AF and AR did not.

-- ALL services should have included.

252.225-7006 **BUY AMERICAN ACT, TRADE AGREEMENTS ACT, AND THE BALANCE OF PAYMENTS PROGRAM** 225.407(a)(2)

-- **Purpose:** Implements subject acts/program.

-- **Applicability:** All solicitations subject to Trade Agreements Act.

-- NV included; AF and AR did not.

-- ALL services should have included.

252.225-7009 **PREFERENCE FOR CERTAIN DOMESTIC COMMODITIES** 225.7002(b)

-- **Purpose:** Limits purchase of specified items (one of which is specialty metals) to domestic products.

-- **Applicability:** In all solicitations expected to have, and all small purchases and contracts which have a value of $10K or more.

-- AF and NV included; AR did not.

-- AR KO may have known item did not contain material defined as "specialty metals" in 225.7001.

252.225-7011 **PREFERENCE FOR DOMESTIC SPECIALTY METALS (MAJOR PROGRAMS)** 225.7002(d)(1)

-- **Purpose:** Limits purchase of specialty metals to dometic products.

-- **Applicability:** In all solicitations and contracts over $10K that call for the delivery to the Government of an article containing specialty metals within the following six major classes of programs: aircraft, missile and space systems, ships, tank-automotive, weapons, and ammunition.

-- AF included; AR and NV did not.

-- Although item does not appear to fall into one the above categories, AF KO may have assumed it did, while AR and NV did not.

252.225-7012 **PREFERENCE FOR DOMESTIC SPECIALTY METALS** 225.7002(d)(2)

-- **Purpose:** Limits purchase of specialty metals to domestic products.

-- **Applicability:** In all solicitations and contracts over $10K that call for the delivery to the Government of an article containing specialty metals, other than those major classes cited in clause 252.225-7001.

-- AF and NV included; AR did not.

-- AF application is inconsistent with clause 252.225-7011 above; should be one or the other if item contains specialty metals. AR KO may have known item did not contain specialty metals.

52.227-1 **AUTHORIZATION AND CONSENT** 27.201-2(a)

-- **Purpose:** Prescribes policy with respect to cases where the Government has authorized or consented to the manufacture or use of an invention described in and covered by a patent of the U.S.

-- **Applicability:** In solicitations and contracts over $25K unless both performance and delivery will be outside the U.S.

-- AF and NV included; AR did not.

-- ALL services should have included.

52.227-2 **NOTICE AND ASSISTANCE REGARDING PATENT AND COPYRIGHT INFRINGEMENT** 27.202-2

-- **Purpose:** States contractor is required to notify the KO of all claims of infringement that come to the contractor's attention in connection with performing a Government contract.

-- **Applicability:** In solicitations and contracts over $25K unless both performance and delivery will be outside the U.S.

-- AF and NV included; AR did not.

-- ALL services should have included.

52.227-3 **PATENT INDEMNITY** **27.203-4(a)(2)**

-- **Purpose:** Covers indemnification of the Government by the contractor for patent infringement liabilities related to commercial items.

-- **Applicability:** Optional in solicitations if the KO determines the supplies normally are or have been sold or offered for sale by any supplier to the public in the commercial open market.

-- AF included; AR and NV did not.

-- Use is optional.

52.230-1 **COST ACCOUNTING STANDARDS NOTICES AND CERTIFICATION (NATIONAL DEFENSE)** **30.201-3**

-- **Purpose:** Allows offerors to (1) certify their disclosure statement status; (2) claim exemption from CAS; (3) certify whether award of the contemplated contract would require a change to existing cost accounting practices.

-- **Applicability:** In solicitations subject to CAS.

-- AF included; AR and NV did not.

-- CAS requirements do not apply to FFP contracts awarded without submission of any cost data (provided that the failure to submit such data is not attributable to a waiver of the requirement for certified cost or pricing data); since hypothetical contract was awarded using competitive procedures and was based on adequate price competition, no cost or pricing data would have been required. Clause is not applicable.

252.231-7000 **SUPPLEMENTAL COST PRINCIPLES** **231.201**

-- **Purpose:** Concerns allowability of costs.

-- **Applicability:** In all solicitations and contracts over $25K.

-- AF and AR included; NV did not.

-- Although 231.201 says "all solicitations and contracts", it can be assumed that since hypothetical contract was awarded using competitive procedures and was based on adequate price competition, no cost or pricing data would have been required; therefore, it would have been unnecessary to address allowability of costs.

52.232-23,ALT I **ASSIGNMENT OF CLAIMS** **32.806(a)(2)**

-- **Purpose:** Prescribes policies and procedures covering the transfer or making over by the contractor to a bank, trust company, or other financing institution, as security for a loan to the contractor, of its right to be paid by the Government for contract performance.

-- **Applicability:** In solicitations and contracts when the contract amount is expected to be $1K or more, unless the contract will prohibit the assignment of claims. ALT I is used when a 'no-setoff' commitment is to be included in the contract. "No-setoff commitment" means a contractual undertaking that, to the extent permitted by the Assignment of Claims Act of 1940, payments by the designated agency to the assignee under an assignment of claims will not be reduced to liquidate the indebtedness of the contractor to the Government. 32.803(d) states a no-setoff commitment may only be included in time of war or national emergency in any contract permitting the assignment of claims.

-- AF and AR included; NV did not.

-- The basic clause 52.232-23, vice ALT I, should have been used by all services.

52.242-10 **FOB ORIGIN - GOVERNMENT BILLS OF LADING OR PREPAID POSTAGE** **42.1404-2(a)**

-- **Purpose:** To advise offerors that transportation/shipping will be on an FOB Origin basis.

-- **Applicability:** In solicitations and contracts when FOB Origin shipments are to be made using Government GBLs or prepaid postage.

-- AF used; AR and NV did not.

-- AF KO determined this was most advantageous to the Government; others methods are available to the Government.

NOTE: AF also included the following companion clauses that cover various FOB ORIGIN situations:

52.247-1	COMMERCIAL BILL OF LADING NOTATIONS	47.104-4(a)
52.247-29	FOB ORIGIN	47.303-1(c)
52.247-47	EVALUATION - FOB ORIGIN	47.305-3(f)(2)
52.247-56	TRANSIT ARRANGEMENTS	47.305-13(a)(3)(ii)
52.247-61	FOB ORIGIN - MINIMUM SIZE OF SHIPMENTS	47.305-16(c)
52.247-60	GUARANTEED MAXIMUM SHIPPING WEIGHTS AND DIMENSIONS	47.305-16(b)(1)

52.242-12 REPORT OF SHIPMENT (RESHIP) 42.1406-2

-- **Purpose:** The advise contractor that the Government requires advance notice of shipments enroute from contractor's plant.

-- **Applicability:** In solicitations and contracts when carload or truckload shipments will be made to DoD installations or, as required, to civilian agency facilities.

-- AR and NV included; AF did not.

-- Apparently, AR and NV required advance notice and assumed shipment of item would be by carload or truckload.

52.244-5 COMPETITION IN SUBCONTRACTING 44.204(e)

-- **Purpose:** To advise contractor that he should select subcontractors (including suppliers) on a competitive basis to the maximum practical extent consistent with the objectives and requirements of the contract.

-- **Applicability:** In solicitations and contracts over $25K, except when a FFP contract, awarded on the basis of adequate price competition.

-- NV included; AF and AR did not.

-- Clause is not applicable.

52.246-23 LIMITATION OF LIABILITY 46.805(a)(1)

-- **Purpose:** Prescribes policies and procedures for limiting contractor liability for loss of or damage to property of the Government that (a) occurs after acceptance and (b) results from defects or deficiencies in the supplies.

-- **Applicability:** In solicitations and contracts over $25K and unit cost of the item is 100K or less; not required when items are priced at or based on catalog or market prices.

-- AR included; AF and NV did not.

-- Apparently, AR assumed unit cost was 100K or less.

52.246-24 LIMITATION OF LIABILITY - HIGH VALUE ITEMS 46.805(a)(2)

-- **Purpose:** Prescribes policies and procedures for limiting contractor liability for loss of or damage to property of the Government that (a) occurs after acceptance and (b) results from defects or deficiencies in the supplies delivered.

-- **Applicability:** In solicitations and contracts over $25K when unit cost of the item is more than $100K; not required when items are priced at or based on catalog or market prices.

-- NV included; AF and AR did not.

-- Apparently, NV assumed unit cost was over $100K. AF did not use either clause. Apparently, since item is commercially available, the AF KO assumed item was priced at or based on catalog or market price.

52.247-34 FOB DESTINATION 47.303-6(c)

-- **Purpose:** To advise offerors that transportation/shipping will be on an FOB Destination basis.

-- **Applicability:** In solicitations and contracts when delivery is on an FOB Destination basis.

-- NV included; AF and AR did not.

-- NV KO determined this was most advantageous to the Government; others methods are available to the Government.

NOTE: NV also included the following companion clauses that cover various FOB DESTINATION situations:

52.247-48	**FOB DESTINATION - EVIDENCE OF SHIPMENT**	47.305-4(c)
52.247-54	**DIVERSION OF SHIPMENT UNDER FOB DESTINATION CONTRACTS**	47.305-11(b)(2)

52.247-52 CLEARANCE AND DOCUMENTATION REQUIREMENTS - SHIPMENTS TO DOD AIR OR WATER TERMINAL TRANSSHIPMENT POINTS 47.305-6(f)(2)

-- **Purpose:** To set forth clearance and documentation responsibilities of the contractor.

-- **Applicability:** In solicitations and contracts when supplies are to move in the Defense Transportation System (DTS) and when shipments are to be made to air or water ports for transshipment to overseas destinations.

-- NV included; AF and AR did not.

-- Apparently, NV anticipated overseas shipment and the others did not.

52.247-57 **TRANSPORTATION TRANSIT PRIVILEGE CREDITS** 47.305-13(b)(4)

-- **Purpose:** To take advantage of any available transit credits offered by contractors.

-- **Applicability:** In solicitations and contracts when supplies are of such a nature, or when it is the custom of trade, that offerors may have potential transit credits available and the Government may reduce transportation costs through the use of transit credits.

-- AF and NV included; AR did not.

-- Apparently, AF and NV KO determined item was of a nature such that transit credits may be available, while the AR did not.

52.247-58 **LOADING, BLOCKING AND BRACING OF FREIGHT CAR SHIPMENTS** 47.305-15(a)(2)

-- **Purpose:** To set forth requirement that contractor must comply with standards published by the Association of American Railroads when shipment is to be made by rail.

-- **Applicability:** In solicitations and contracts when supplies may be shipped in carload lots by rail.

-- NV included; AF and AR did not.

-- Apparently, NV anticipated the possibility that items would be shipped by rail, while AF and AR did not.

52.247-64 **PREFERENCE FOR PRIVATELY OWNED U.S. - FLAG COMMERCIAL VESSELS** 47.507(a)

-- **Purpose:** To set forth the requirements of the Cargo Preference Act of 1954.

-- **Applicability:** In solicitations and contracts that may involve ocean transportation of supplies.

-- AR included; AF and NV did not.

-- Apparently, AR anticipated posibility of ocean transportation, while the AF and NV did not.

52.248-1 VALUE ENGINEERING 48.201(b)

-- **Purpose:** To provide a value engineering incentive.

-- **Applicability:** In solicitations and contracts when the contract amount is expected to be $100K or more. One of several exceptions is for commercial products that do not involve packaging specifications or other special requirements or specifications.

-- NV included; AF and AR did not.

-- Since hypothetical parameters did not address it, apparently NV assumed there were packaging specifications or other special requirements; AF and AR did not.

52.252-6 AUTHORIZED DEVIATIONS IN CLAUSES 52.107(f)

-- **Purpose:** To advise offerors that some clauses may contain authorized deviations to language in FAR.

-- **Applicability:** In solicitations and contracts that include and FAR or supplemental clause with an authorized deviation.

-- AF included; AR and NV did not.

-- Apparently, AF has obtained deviations while AR and NV have not.

SUBMITTED BY THE BOEING COMPANY

June 21, 1989

WHITE PAPER ON COMMERCIAL PRACTICES IN GOVERNMENT PROCUREMENT (DRAFT)

This paper provides further information concerning the problem clauses shown on the spares basic ordering agreement (BOA) matrix. Attachment I to this paper contains a detailed description of the barriers presented by each clause with respect to the Government's procurement of commercial products. Attachment I does not contain an exhaustive listing of all the clauses, regulations, certificates, etc., applicable to doing business with the Government. There are other clauses that industry would consider problems in the context of procurement of commercial products, and these can be addressed at a later time.

Before getting into the details we would like to make several recommendations that would go a long way toward ameliorating the problems a commercial contractor encounters in sales to the U.S. Government. First, we recommend that there be a comprehensive definition of "commercial product". We believe a "commercial product" should include not only a product currently being sold or offered for sale to the general public, such as a commercial aircraft or spare part for such aircraft, but also modifications to such products of the kind or type that are regularly requested by the commercial customers, e.g., an increase in gross weight thereby enabling the aircraft to carry more fuel and fly farther.

Second, we recommend that the Government establish a single FAR test to determine whether a product qualifies as a "commercial product." On page 9 of Attachment I we give an example of such a test keying off of the catalog or market price exemptions. Once a product satisfies the test, procurements of the product would be exempt from those Government regulations that are inconsistent with commercial terms, including those requiring flowdown to vendors and suppliers.

Third, we recommend that FAR be modified to recognize that in those situations where the Government acquisition includes materials, parts, subassemblies, and components that have been routinely produced and ordered by a contractor as part of its ongoing commercial activities, the orders issued to suppliers and vendors of the prime contractor shall not be considered "subcontracts" for purposes of flow down of Government terms and conditions.

We have grouped the problems into several categories as set forth below. Since the same problem may have a slightly different impact depending upon whether the commercial contractor is a prime contractor, or a subcontractor, the impact for each is described separately, where appropriate. Attachment II gives a complete listing of the matrix clauses by category.

I. FLOWDOWN AND PRE-EXISTING COMMERCIAL SOURCING DECISIONS

A. Pre-Existing Sourcing Decisions

A significant problem faced by a commercial prime or a subcontractor is the inability to comply with Government-unique terms and conditions where pre-existing sourcing decisions have already been made. Generally prior to a Government's order or solicitation for a commercial product, sourcing decisions of every kind have been made and in many cases procurement is already underway using standard commercial arrangements to satisfy long-term projected sales requirements. The contractor thus has no ability to manufacture or procure the commercial product pursuant to Government-unique terms and conditions that are imposed on a prime contractor and in some cases, flowed down to a subcontractor.

B. Flowdown

Prime contractors are in some cases required by either law or regulation, to flowdown certain terms and conditions to the subcontractor. In other cases, the prime contractor will flowdown government terms and conditions to its subcontractors in order to ensure complete compliance with prime contractual requirements. As indicated above, compliance with Government requirements may be impossible where sourcing decisions have long been made. In some cases where sourcing decisions have not already been made, (i.e., there is more than one possible source for the particular source, or procurement is not already underway,) flowdown is possible but not practical. It is not practical because of the tremendous administrative burden placed upon both the commercial contractor and its vendors and suppliers to adjust to the Government-unique requirements, disrupting their respective commercial production activities. The result is an increase in product and administrative costs that jeopardizes the catalog or market price. The catalog or commercial market price and commercial delivery flow times are based on standard commercial practices and do not take into account changes introduced by the Government unique requirements. To further complicate the matter, many of these commercial vendors refuse to accept the Government-unique terms and conditions which could leave a prime contractor without sources for necessary components or spare parts. Under such circumstances, the government must determine whether or not such additional requirements and associated loss of the "commercial" benefits (including both the cost and schedule benefits) are justified.

Clauses which illustrate these problems include:

FAR § 52.246-2, INSPECTION OF SUPPLIES - FIXED PRICE

FAR § 52.208-1, REQUIRED SOURCES FOR JEWEL BEARINGS AND RELATED ITEMS

DFARS § 252.208-7003, REQUIRED SOURCES FOR HIGH CARBON FERROCHROME (FCH)

II. FINANCIAL/AUDIT

This category covers several different problems: (1) disclosure of competitive sensitive financial data, (2) the submission of "cost and pricing data" and the attendant administrative burdens caused by various Government-unique reporting and data collection requirements, and (3) provisions requiring adjustments to established catalog or commercial market prices.

We find that commercial contractors and their vendors or suppliers will forego Government business to avoid the risk of exposing competitive sensitive and confidential financial information. Many FAR provisions provide broad audit rights to the financial books and records of a commercial contractor and its vendors and suppliers. There is no apparent way to limit the scope of the audit to books and records related only to the sales history of a commercial product.

In addition, to require a commercial contractor and its vendors or suppliers to collect and submit "cost or pricing data" in many cases means a substantial modification to their financial system. This is because commercial accounting standards are generally not compatible with the Government-unique record keeping and cost accounting requirements. Commercial businesses who want to sell their commercial products to the Government without having to submit such data may be exempt by reason of the price competition or catalog price exemptions. However, the restrictive interpretations of what constitutes a catalog or market price make it difficult to obtain the desired exemption. The catalog price exemption is available when the negotiated price is based on established catalog or market prices of commercial items sold in substantial quantities to the general public. Because the term, "substantial quantities" has not been precisely defined (quantity "sufficient to constitute a real commercial market"), Government procurement personnel are encouraged to use a formula calculating a percentage of sales to determine whether or not to grant an exemption. It is this "percentage of sales" calculation which causes the problems for many commercial contractors and their suppliers and vendors.

In addition, Government procurement personnel often narrowly interpret what constitutes a price competition and require cost or pricing data even when it is not appropriate which would otherwise provide an exemption from submission of such data.

Another area of concern are the FAR provisions used in commercial procurements which require price adjustments. Use of these clauses are inappropriate when dealing with catalog or market prices that are established.

Clauses which illustrate these problems include:

FAR § 52.215-2, AUDIT NEGOTIATION

FAR § 52.229-4, FEDERAL, STATE, AND LOCAL TAXES

FAR SUPP § 252.225-7007, SUPPLIES TO BE ACCORDED DUTY FREE ENTRY

FAR § 52.215-22, PRICE REDUCTION FOR DEFECTIVE COST OR PRICING DATA

FAR § 52.215-1, EXAMINATION OF RECORDS BY COMPTROLLER GENERAL

III. STATUTORY AND/OR REGULATORY OVERLAP/INTERFERENCE WITH COMMERCIAL PRODUCTION PRACTICES

A commercial contractor doing business in the private sector is subject to a variety of laws, regulations, and contractual commitments applicable to its commercial sales. If government clauses, standards and specifications impose technical, sourcing and/or scheduling requirements that are inconsistent with these requirements, it can cause a significant impact to production and factory requirements, and in some cases sale of the product to the government may become technically and/or economically impossible. In such instances, costs would be increased and schedules would be delayed or programs would be terminated, without any apparent, added benefit to the government. When such situations exist, the government must determine whether or not such additional or conflicting requirements justify the loss of "commercial" benefits.

Clauses which illustrate these problems include:

FAR § 52.212-8, DEFENSE PRIORITY AND ALLOCATION REQUIREMENTS

FAR § 52.210-7, USED OR RECONDITIONED MATERIAL RESIDUAL INVENTORY AND FORMER GOVERNMENT SURPLUS PROPERTY

FAR § 52.244-5, COMPETITION IN SUBCONTRACTING

DFARS § 252.223-7000, NOTICE OF RADIOACTIVE MATERIALS

DFARS § 252.225-7017, LIMITATION OF SALES COMMISSIONS AND FEES FOR FOREIGN GOVERNMENTS

FAR § 52.223-1, -2, CLEAN AIR & WATER

IV. DATA RIGHTS

The requirements imposed by the government in the area of technical data greatly impact the procurement of commercial products. One of the major obstacles to commercial contractors seeking to compete in the government marketplace is the regulatory limitation imposed on their ability to protect proprietary rights in technical data and computer software. A commercial contractor invests significant resources in developing competitive commercial processes and products. The competitive advantage resulting from the "uniqueness" of such processes and products is essential to the contractor's success in its commercial markets. To require contractors to relinquish rights in their proprietary information and/or computer software, either as an express condition of competing or as an inevitable result of being the successful bidder, in order to satisfy second source competition requirements fails to recognize and compensate the contractor for this investment. For the Government to acquire rights to a commercial contractor's property interests in data merely because it is required to perform a contract is inequitable and inconsistent with statutory requirements. In the long run this could significantly affect a contractor's interest in privately funding the development of new commercial products and processes or could dissuade a contractor from bidding on government contracts.

In order to have any chance to protect commercially valuable proprietary data and computer software, current government procurement regulations would require the commercial contractor to keep records to prove private expense development of the commercial product. This approach is unfair and unworkable because it requires a commercial contractor to incur the expense of generation and storage of voluminous records, possibly for many years before the government has any interest in the commercial product. Thus, a commercial contractor who incurs the added costs associated with generating and storing such development records will find itself at a competitive disadvantage in the commercial marketplace with respect to a competitor who refuses to do business with the government and, accordingly, never incurs such costs.

Clauses which illustrate these problems include:

FAR § 52.203-6, RESTRICTIONS ON SUBCONTRACTOR SALES TO THE GOVERNMENT

DFARS § [illegible] 227-7013, RIGHTS IN TECHNICAL DATA AND COMPUTER SOFTWARE (Not in BOA matrix)

Attachment I

DETAILED DESCRIPTION OF BARRIERS

Clauses Found in the Commercial-Common Spare Parts BOA Matrix Dated May 5, 1989

B-900 SUPPLIES TO BE ORDERED (Contract Special Provision)

Objection to this clause is not based on any "commerciality" issues, but rather resulted from a desire to rewrite the clause in a manner which accurately reflected the type of goods which could be ordered under the BOA contract. Apparently, any revision to this clause requires a waiver.

E-1 INSPECTION OF SUPPLIES - FIXED PRICE. FAR § 52.246-2 IAW § 48.302

In a commercial environment, inspection rights of a buyer are usually those described in the Uniform Commercial Code (UCC). Under the UCC, the buyer may inspect the goods at any reasonable place or time and in any reasonable manner prior to payment or acceptance. "Reasonableness" is defined in terms of custom of the trade, past practices of the parties and other relevant circumstances.

Under this clause, the Government is given rights which far exceed those generally provided to commercial customers. For instance, the Government is given the broad right to inspect in any manner or detail and with as great a frequency as it desires. In addition, the contractor is required to maintain an inspection system which meets Government approval. As part of this system, the contractor must maintain for Government review, records and test results of the inspection system. This extensive oversight and control by Government inspectors result in increased costs, not projected in commercial catalog or market prices, both in terms of complying with the requirements and in terms of the disruptive impact to the contractor's commercial production line, i.e., schedule, work arounds, etc.

G110 CONTRACTOR REPORTING REQUIREMENTS AFLC FAR SUPP § 52.212-9000 IAW § 12.304(90)

The objection to this clause relates to the present practices surrounding the underlying Defense Priorities and Allocations System (DPAS). This particular clause merely imposes the burden of making a copy of a required report and forwarding it to two Government employees rather than one.

H-41 CHANGES IN EXECUTIVE ORDER OR STATUTES. AFLC FAR § SUPP 52.216-9012 IAW § 16.703

This clause allows for unilateral changes by the Government without consideration to the commercial contractor. Commercial transactions generally do not give the buyer the right to unilaterally modify or impose new or additional requirements which is what this clause effectively gives the Government. In addition, the clause fails to provide to the commercial contractor those contractual rights generally available in a commercial transaction under such circumstances, those being: contractor's right to (1) refuse an order, (2) equitable adjustment, and (3) terminate the contract.

H-42 DESIGN CHANGES. AFLC FAR SUPP § 52.217-9026 IAW § 17.7203-90

This is a question of applicability of this clause to the BOA - not a "commerciality" issue.

H-180 SUPPLIES TO BE ACCORDED DUTY FREE ENTRY. FAR SUPP § 252.225-7007 IAW § 252.225-605

IA-292 DUTY FREE ENTRY QUALIFYING COUNTRY END PRODUCTS AND SUPPLIES. DFARS § 252.225-7008

IA-296 DUTY FREE ENTRY - ADDITIONAL PROVISIONS. DFARS § 252.225-7014

H-311 DUTY FREE ENTRY. FAR § 52.225-10

I-353 FEDERAL, STATE, AND LOCAL TAXES. FAR § 52.229-4

IA-648 PRICING OF ADJUSTMENTS. DFARS § 252.243-7001

In a commercial environment, (1) sourcing decisions have already been made and, in many cases, procurement is already underway, and (2) the catalog or class exemption prices are already established. To obtain the benefits of catalog prices, adjustments cannot be accomplished as a result of those requirements imposed by these provisions.

I-21 RESTRICTIONS ON SUBCONTRACTOR SALES TO THE GOVERNMENT, FAR § 52.203-6

This clause presents a flowdown problem. It may be deemed acceptable at the prime contract level by a commercial contractor, although there is some doubt as to the scope of the relief granted by the phrase "might otherwise be authorized by law or regulation." Some commercial contractors may choose not to bid on a Government contract to avoid the possibility that such phrase will or could preclude them from protecting their valuable proprietary rights in commercially sensitive technical data when obtaining the necessary material, components, etc., from their commercial vendors. Clarification in the regulation is required.

I-22 ANTI-KICKBACK PROCEDURES, FAR § 52.203-7

This presents a flowdown problem. Source selections have already been made and, in most instances, procurement is already underway using commercial standard terms to satisfy long-term projected commercial sales requirements. Thus, after-the-fact imposition of this clause cannot be done.

I-61 REQUIRED SOURCES FOR JEWEL BEARINGS AND RELATED ITEMS, FAR § 52.208-1

IA-76 REQUIRED SOURCES FOR MINIATURE AND INSTRUMENT BALL BEARINGS, DFARS § 252.208-7000

IA-77 REQUIRED SOURCES FOR PRECISION COMPONENTS FOR MECHANICAL TIME DEVICES, DFARS § 252.208-7001

IA-79 REQUIRED SOURCES FOR HIGH CARBON FERROCHROME (FCH), DFARS § 252.208-7003

IA-287 BUY AMERICAN ACT AND BALANCE OF PAYMENTS PROGRAM, DFARS § 252.225-7001

IA-291 BUY AMERICAN ACT, TRADE AGREEMENT ACT AND THE BALANCE OF PAYMENT PROGRAM, DFARS § 252.225-7006

IA-306 RESTRICTION ON CONTRACTING WITH TOSHIBA OR KONGSBERG VAPENFABRIKK, DFARS § 252.225-7011

IA-288 QUALIFYING COUNTRY SOURCES AS SUBCONTRACTORS, DFARS § 252.225-7002

IA-294 PREFERENCE FOR DOMESTIC SPECIALTY METALS (MAJOR PROGRAMS), DFARS § 252.225-7011

IA-295 PREFERENCE FOR DOMESTIC SPECIALTY METALS, DFARS § 252.225-7012

These clauses present pre-existing source selection or flowdown problems. When the Government procures a commercial product, commercial requirements have preceded the Government's solicitation or order. This means that sourcing decisions have already been made and, in many cases, actual procurement activity is already underway using commercial practices, terms, standards and conditions. This is done in order to satisfy long-term projected commercial sales requirements. The commercial contractor thus has no ability to manufacture or procure using unique Government terms, conditions, and specifications. Even where opportunity for adjustments (if acceptable) to vendor and suppliers standard commercial business arrangements are possible, the impact is too severe to be practical (involves three to four thousand suppliers and vendors).

I-83 NEW MATERIAL, FAR § 52.210-5

I-84 USED OR RECONDITIONED MATERIAL RESIDUAL INVENTORY AND FORMER GOVERNMENT SURPLUS PROPERTY, FAR § 52.210-7

In a commercial sale, Federal Aviation Administration (FAA) regulations govern these requirements and would appear to be in conflict with these clauses. Commercial procedures are established pursuant to FAA requirements allowing the use of what are termed "serviceable parts" to accommodate such things as "Aircraft On Ground" (AOG) and certain other requirements. These clauses would prohibit the use of such parts or, at a minimum, raise questions about their use. Emergency situations could not be accommodated satisfactorily as they are today with commercial customers.

I-102 DEFENSE PRIORITY AND ALLOCATION REQUIREMENTS (DPAS), FAR § 52.212-8

DPAS, as interpreted today, permits Government procurement personnel to set a delivery date for their commercially acquired products which takes precedence over sales to commercial customers. To give the prerogative to accelerate a delivery date that takes precedence over sales to commercial customers, other than for national security reasons, unnecessarily jeopardizes commercial schedules and programs. In a commercial environment where sales to multiple customers exist, it is not feasible to contract to such potential disruption. The interests of the Government are protected by other statutes and regulations in the event of a national emergency. The problem is often one of interpreting the rights of the Government far more narrowly than the clause provides - clarification is needed.

I-127 EXAMINATION OF RECORDS BY COMPTROLLER GENERAL, FAR § 52.215-1

I-128 AUDIT NEGOTIATION, FAR § 52.215-2

These clauses, when applied to commercial transactions, expose to Government audit commercial contractors' books and records. There is no apparent way to limit the scope of the audit to books and records related to the sales history of that commercial part or parts to be delivered under a Government contract. For this reason, commercial contractors are unwilling to expose themselves to the risk that competitive sensitive and confidential financial information could be disclosed to a competitor, to support Government-connected business. The fundamental purpose of the Government's right to audit a contractor's books and records is to assure that costs reported by a contractor were actually incurred and that they were reasonable. This requirement is understandable when dealing with cost-type contracts for Government-peculiar items. However, such authority is inappropriate for commercial contractors selling products whose prices are determined by the forces of a competitive commercial market.

I-228 UTILIZATION OF LABOR SURPLUS AREA CONCERNS, FAR § 52.220-3

I-229 LABOR SURPLUS AREA SUBCONTRACTING PROGRAM, FAR § 52.220-4

I-274 AFFIRMATIVE ACTION SPECIAL DISABLED AND VIETNAM ERA VETERANS, FAR § 52.222-35.

I-276 AFFIRMATIVE ACTION FOR HANDICAPPED WORKERS, FAR § 52.222-36

In large companies having military divisions performing Government contracts, these requirements are generally complied with. In smaller companies whose business is solely or primarily commercial, these clauses may present a compliance problem at the prime level. In either case, these clauses also present flowdown problems. When the Government procures a commercial product, commercial requirements have preceded the Government's solicitation or order. This means that sourcing decisions have already been made and, in many cases, actual procurement activity is already underway using commercial standard terms, conditions, specifications and procedures. This is done in order to satisfy long-term projected commercial sales requirements. The commercial contractor thus has no ability to manufacture or procure using unique Government requirements.

I-278 EMPLOYMENT REPORTS ON SPECIAL DISABLED VETERANS AND VETERANS OF THE VIETNAM ERA. FAR § 52.222-37

Commercial contractors are not required to routinely issue such reports and do not require their commercial vendors to do so. This clause presents flowdown problems. When the Government procures a commercial product, commercial requirements have preceded the Government's solicitation or order. This means that sourcing decisions have already been made and, in many cases, actual procurement activity is already underway using commercial standard terms. This is being done in order to satisfy long-term projected commercial sales requirements. The commercial vendor thus has no ability to manufacture or procure using unique Government terms, conditions and specifications.

I-317 NOTICE AND ASSISTANCE REGARDING PATENT AND COPYRIGHT INFRINGEMENTS. FAR § 52.227-2

In a commercial environment, sourcing decisions have already been made and, in many cases, procurement is already underway. Neither the Authorization and Consent clause (FAR § 52.227-1) nor this clause offer any benefit to a commercial contractor who must compete in the commercial market for all of its commercial sales, without the "benefit" of a Government authorization to infringe another's patent(s). The Government's interests are protected because it is unlikely that the conditions under which these clauses generally apply, will occur when buying commercial products.

I-573 COMPETITION IN SUBCONTRACTING. FAR § 52.244-5

There are several reasons why imposition of this clause for the procurement of commercial products is inappropriate. First, source selection has already been made, and procurement is already underway using commercial competition practices to satisfy long-term projected commercial sales requirements well in advance of the Government order or solicitation. Second, the commercial acquisition system is not set up where each order is competed when received from a customer. Finally, commercial contractors do not routinely place an order with a vendor based solely on the lowest price, but rather will also equally consider quality, schedule, reliability and other factors. The Government regulations interpreting the CICA law presently make the lowest price the primary consideration. This fails to give appropriate consideration to all qualifying elements of a subcontractor's anticipated performance.

IA-22 SPECIAL PROHIBITION ON EMPLOYMENT, § DFARS 52.203-7001

This clause is acceptable to contractors at the prime level. However, with respect to flowdown, in a commercial environment, sourcing decisions have already been made and, in many cases, procurement is already underway using commercial standard terms to satisfy long-term projected commercial sales requirements well in advance of the Government order or solicitation. The commercial vendor thus has no ability to manufacture or procure the spares item pursuant to Government-unique terms.

IA-270 NOTICE OF RADIOACTIVE MATERIALS, DFARS § 252.223-7000

Licensing requirements for radioactive material are governed by regulations issued pursuant to The Atomic Energy Act of 1954, as amended. A commercial contractor in doing business in the private sector is already required to comply with this Act, as well as OSHA requirements, and in the aviation industry, the requirements of the Federal Aviation Administration (FAA). The interests of the Government are protected without the additional costly requirements of complying with this clause. Such overlap results in increased costs not projected in catalog or commercial market prices. Under such circumstances, the Government must determine whether or not such additional requirements and associated loss of the "commercial" benefits (including the cost and schedule benefits) are justified.

IA-271 SAFETY PRECAUTIONS FOR AMMUNITION AND EXPLOSIVES, DFARS § 52.223-7001

IA-272 CHANGE IN PLACE OF PERFORMANCE - AMMUNITION AND EXPLOSIVES, DFARS § 252.223-7002

A commercial contractor doing business in the private sector is already required to comply with OSHA requirements, and, in the aviation industry, the applicable requirements of the Federal Aviation Administration (FAA). The interests of the Government are thus protected without the additional, burdensome requirements of complying with this clause. Such overlap results in increased costs, not projected in catalog or commercial market prices. Under such circumstances, the Government must determine whether or not such additional requirements and associated loss of the "commercial" benefits (including the cost and schedule benefits) are justified.

IA-298 LIMITATION OF SALES COMMISSIONS AND FEES FOR FOREIGN GOVERNMENTS, DFARS § 252.225-7017

A commercial contractor doing business in the private sector is already required to comply with laws applicable to the use of foreign sales consultants in their commercial business, e.g., the Foreign Corrupt Practices Act. The interests of the Government are thus protected without the additional, potentially conflicting, and thus burdensome, requirements of complying with this clause.

K-52 SALES HISTORY IAW FAR § 11.006

The application of this certificate is inconsistent with the intent of the FAR. In the case of commercial products being offered under a commercial catalog and/or "class" exemption, the determination has already been made that the goods qualify as a "commercial" or "commercial-type" product. If such a certificate is to be required at all, it should be required only once, to verify that the catalog/class exemption has, in fact, been obtained. In a procurement involving multiple orders, such as a Basic Ordering Agreement, it would be unduly burdensome and duplicitous to have to certify for each part number involved in that procurement when that part, component, or system has already satisfied the catalog or class price exemption. In at least one situation, the agency has insisted that the certification be provided with each part ordered under a commercial basic ordering agreement for spare parts, notwithstanding the existence of a class exemption from the cognizant ACO.

K-70 CERTIFICATE OF COMMERCIAL PRICING, AFLC § 52.215-9009

The statute is a disclosure statute. Some agencies have adopted a view that overreaches the requirements of the statute precluding contractors from disclosing and excluding (in a practical manner) certain classes of sales that are based on different terms from operation of the certificate. What is needed for a BOA is authority for advanced agreements excluding certain sales from the certificate on a continuing basis rather than having to secure the exclusion on an order-by-order basis. This continues to create significant problems for commercial vendors attempting to do business with the Government because compliance with the regulation impacts schedules and significantly increases administrative burdens with little or no benefit to the Government. This clause could effectively render the use of a BOA impractical.

DETAILED DESCRIPTION OF BARRIERS

Additional Clauses Found in an Earlier Version of the BOA Matrix but Excluded From the May 5, 1989 Version

SUBCONTRACTOR COST OR PRICING DATA, FAR § 52.215-24

SUBCONTRACTOR COST OR PRICING DATA - MODS, FAR § 52.215-25

PRICE REDUCTION FOR DEFECTIVE COST OR PRICING DATA, FAR § 52.215-22

PRICE REDUCTION FOR DEFECTIVE COST OR PRICING DATA - MODS, FAR § 52.215-23

To require a commercial contractor and its vendors or suppliers to collect and submit "cost or pricing data" in many cases means a substantial modification to their financial system. This is because commercial accounting standards are generally not compatible with the Government-unique record keeping and cost accounting requirements. Commercial businesses who want to sell their commercial products to the Government without having to submit such data may be exempt by reason of the price competition or catalog price exemptions. However, Government procurement personnel often narrowly interpret what constitutes a price competition and require cost or pricing data even when it is not appropriate which would otherwise provide an exemption from submission of such data. In addition, the restrictive interpretations of what constitutes a catalog or market price make it difficult to obtain the desired exemption. The catalog price exemption is available when the negotiated price is based on established catalog or market prices of commercial items sold in substantial quantities to the general public. Because the term, "substantial quantities" has not been precisely defined (quantity "sufficient to constitute a real commercial market"), Government procurement personnel are encouraged to use a formula calculating a percentage of sales to determine whether or not to grant an exemption. It is this "percentage of sales" calculation which causes the problems for many commercial contractors and their suppliers and vendors.

For instance, it is not uncommon for commercial businesses to sell products as part of a system without individually pricing that system's components and each system can be unique to each customer's requirements. The end result is that the system is not a single catalog item that satisfies the Government's present commerciality definition and neither is the system composed of component items that satisfy the test. Another problem involves new products for which the commercial contractor has yet to achieve the sufficient percentage range required for an exemption. Yet another problem arises when the Government procures a commercial product in greater quantities as compared to the quantities consistently sold to commercial customers which "skews" the percentages so that the products fall outside the acceptable range to obtain the exemption (even though the product is still being sold in the same quantities to the general public.)

To ameliorate these types of problems we recommend the Government establish a single FAR test to determine whether a product constitutes a "commercial product". This test should include not only those products which have been sold in substantial quantities to the general public, but also those (1) modified commercial products, where the modifications being bought by the Government are identical or similar to modifications regularly made, or offered to be made, to the product in the contractor's normal, commercial markets; (2) discontinued commercial products where the product is no longer in production for its commercial market, but for which spare parts continue to be sold in substantial quantities to the general public; and (3) new commercial products, where the product has been introduced and offered for sale in a commercial market, (i.e., to be regularly used for other than Government purposes by the general public), but for which "substantial" commercial orders, shipments, etc., have not been achieved.

UTILIZATION OF SMALL BUSINESS CONCERNS AND SMALL DISADVANTAGED BUSINESS CONCERNS, FAR § 52.219-8

SMALL BUSINESS AND SMALL DISADVANTAGED BUSINESS SUBCONTRACTING PLAN, FAR § 52.219-9

In large companies having military divisions performing Government contracts, these requirements are generally complied with. In smaller companies whose business is solely or primarily commercial, this presents a compliance issue at the prime level. In either case, these clauses also present flowdown problems. When the Government procures a commercial product, commercial requirements have preceded the Government's solicitation or order. This means that sourcing decisions have already been made and, in many cases, actual procurement activity is already underway using commercial standard terms. This is being done in order to satisfy long-term projected commercial sales requirements. The commercial vendor thus has no ability to manufacture or procure using unique Government terms, conditions and specifications. Accordingly, no "further subcontracting opportunities exist". The FAR should be changed to acknowledge that no subcontracting opportunities exist when a product meets the "Commercial Product" definition.

CERTIFICATION OF NONSEGREGATED FACILITIES, FAR § 52.222-21

EQUAL OPPORTUNITY, FAR § 52.222-26

In large companies having military divisions performing Government contracts, these requirements are generally complied with. In smaller companies whose business is solely or primarily commercial, this presents a compliance issue at the prime level. In either case, these clauses also present flowdown problems. When the Government procures a commercial product, commercial requirements have preceded the Government's solicitation or order. This means that sourcing decisions have already been made and, in many cases, actual procurement activity is already underway using commercial standard terms. This is being done in order to satisfy long-term projected commercial sales requirements.

The commercial vendor thus has no ability to manufacture or procure using unique Government terms, conditions and specifications. Accordingly, no "further subcontracting opportunities exist".

CLEAN AIR & WATER, FAR § 52.223-1, -2

A commercial contractor in doing business in the private sector is already required to comply with laws applicable to the commercial business, i.e., the Clean Air Act and the Clean Water Act. To the extent that the regulation is consistent with the requirements of the law, the interests of the Government are protected by the law and the regulation is unnecessary. To the extent that the regulation differs from the law, it unnecessarily imposes additional and/or conflicting, burdensome requirements. This can result in increased costs not projected in catalog or commercial market prices. Under such circumstances, the Government must determine whether or not such additional requirements and associated loss of the "commercial" benefits (including the cost and schedule benefits) are justified.

COST ACCOUNTING STANDARDS, FAR § 52.230-3

ADMINISTRATION OF COST ACCOUNTING STANDARDS, FAR § 52.230-4

Imposition of these clauses would require any commercial business to substantially modify its financial system - commercial accounting standards which are not compatible with the Government-unique record keeping and cost accounting requirements. For commercial businesses who are solely or primarily commercial-oriented, imposition of these requirements require a business to either substantially revise its present system to accommodate the Government-unique features, or to establish a parallel system, both which are equally administratively burdensome and increase costs without added benefit to the Government. Contractors who want to sell to the Government but will not be able to comply with the Cost Accounting Standards can attempt to qualify for a commercial exemption from compliance with the requirements of this accounting system. It is the restrictive interpretation, however, which is applied to this exemption by procurement personnel which makes it troublesome, if not impossible, for a commercial contractor to obtain such exemption for its commercial product(s) because it fails to take into account established commercial systems and pricing methods.

PREFERENCES FOR CERTAIN DOMESTIC COMMODITIES, DFARS § 252.225-7009

PREFERENCE FOR PRIVATELY OWNED U.S.-FLAG COMMERCIAL VESSELS, FAR § 52.247-64

These clauses present a pre-existing source decisions and flowdown problems. When the Government procures a commercial product, commercial requirements have preceded the Government's solicitation or order. This means that sourcing decisions have already been made and, in many cases, actual procurement activity is already underway using commercial practices, terms, standards and conditions. This is done in order to satisfy long-term projected commercial sales requirements. The commercial contractor thus has no ability to manufacture or procure using unique Government terms, conditions, and specifications.

Attachment II

DETAILED CATEGORIZED LIST (BY TITLE)

Clauses Found in the Commercial-Common Spare Parts BOA Matrix Dated May 5, 1989

I. FINANCIAL/AUDIT

E-1 INSPECTION OF SUPPLIES - FIXED PRICE, FAR 52.246-2 IAW 48.302

H-41 CHANGES IN EXECUTIVE ORDER OR STATUTES, AFLC FAR SUPP 52.216-9012 IAW 16.703

H-180 SUPPLIES TO BE ACCORDED DUTY FREE ENTRY, FAR SUPP 252.225-7007 IAW 252.225-605

I-21 RESTRICTIONS ON SUBCONTRACTOR SALES TO THE GOVERNMENT, FAR 52.203-6

I-127 EXAMINATION OF RECORDS BY COMPTROLLER GENERAL, FAR 52.215-1

I-128, AUDIT NEGOTIATION, FAR 52.215-2

I-311 DUTY FREE ENTRY, FAR 52.225-10

I-353 FEDERAL, STATE, AND LOCAL TAXES, FAR 52.229-4

IA-292 DUTY FREE QUALIFYING COUNTRY END PRODUCTS AND SUPPLIES, DFARS 252.225-7008

IA-296 DUTY FREE ENTRY - ADDITIONAL PROVISIONS, DFARS 252.225-7014

IA-648 PRICING OF ADJUSTMENTS, DFARS 252.243-7001

K-52 SALES HISTORY IAW FAR 11.006

K-70 CERTIFICATE OF COMMERCIAL PRICING, AFLC FAR SUPP 52.215-9009

II. FLOWDOWN AND PRE-EXISTING COMMERCIAL SOURCING DECISIONS

E-1 INSPECTION OF SUPPLIES -FIXED PRICE, FAR 52.246-2 IAW 48.302

G110 CONTRACTOR REPORTING REQUIREMENTS AFLC FAR SUPP 52.212-9000 IAW 12.304(90)

H-41 CHANGES IN EXECUTIVE ORDER OR STATUTES, AFLC FAR SUPP 52.216-9012 IAW 16.703

H-180 SUPPLIES TO BE ACCORDED DUTY FREE ENTRY, FAR SUPP 252.225-7007 IAW 252.225-605

I-21 RESTRICTIONS ON SUBCONTRACTOR SALES TO THE GOVERNMENT, FAR 52.203-6

I-22 ANTI-KICKBACK PROCEDURES

I-61 REQUIRED SOURCES FOR JEWEL BEARINGS AND RELATED ITEMS, FAR 52.208-1

I-83 NEW MATERIALS, FAR 52.210-5

I-84, USED OR RECONDITIONED MATERIAL RESIDUAL INVENTORY AND FORMER GOVERNMENT SURPLUS PROPERTY, FAR 52.210-7

I-102 DEFENSE PRIORITY AND ALLOCATION REQUIREMENTS, FAR 52.212-8

I-127 EXAMINATION OF RECORDS BY COMPTROLLER GENERAL, FAR 52.215-1

I-128 AUDIT NEGOTIATION, FAR 52.215-2

I-228 UTILIZATION OF LABOR SURPLUS AREA CONCERNS, FAR 52.220-3

I-229 LABOR SURPLUS AREA SUBCONTRACTING PROGRAM, FAR 52.220-4

I-274 AFFIRMATIVE ACTION SPECIAL DISABLED AND VIETNAM ERA VETERANS, FAR 52.222-35

I-276 AFFIRMATIVE ACTION FOR HANDICAPPED WORKERS, FAR 52.222-36

I-278 EMPLOYMENT REPORTS ON SPECIAL DISABLED VETERANS AND VETERANS OF THE VIETNAM ERA, FAR 52.222-37

I-311 DUTY FREE ENTRY, FAR 52.225-10

I-317 NOTICE AND ASSISTANCE REGARDING PATENT AND COPYRIGHT INFRINGEMENTS, FAR 52.227-2

IA-76 REQUIRED SOURCES FOR MINIATURE AND INSTRUMENT BALL BEARINGS, DFARS 252.208-7000

IA-77 REQUIRED SOURCES FOR PRECISION COMPONENTS FOR MECHANICAL TIME DEVICES, DFARS 252.208-7001

IA-79 REQUIRED SOURCES FOR HIGH CARBON FERROCHROME (FCH), DFARS 252.208-7003

IA-270 NOTICE OF RADIOACTIVE MATERIALS, DFARS 252.223-7000

IA-271 SAFETY PRECAUTIONS FOR AMMUNITION AND EXPLOSIVES, DFARS 252.223-7001

IA-272 CHANGE IN PLACE OF PERFORMANCE - AMMUNITION AND EXPLOSIVES, DFARS 252.223-7002

IA-292 DUTY FREE ENTRY QUALIFYING COUNTRY END PRODUCTS AND SUPPLIES, DFARS 252.225-7008

IA-294 PREFERENCE FOR DOMESTIC SPECIALTY METALS (MAJOR PROGRAMS), DFARS 252.225-7011

IA-295 PREFERENCE FOR DOMESTIC SPECIALTY METALS, DFARS 252.225-7012

IA-296 DUTY FREE ENTRY - ADDITIONAL PROVISIONS, DFARS 252.225-7014

IA-22 SPECIAL PROHIBITION ON EMPLOYMENT, DFARS 52.203-7001

IA-287 BUY AMERICAN ACT AND BALANCE OF PAYMENTS PROGRAM, DFARS 252.225-7001

IA-291 BUY AMERICAN ACT, TRADE AGREEMENT ACT AND THE BALANCE OF PAYMENT PROGRAM, DFARS 252.225-7006

III. STATUTORY AND/OR REGULATORY OVERLAP/INTERFERENCE WITH COMMERCIAL PRODUCTION PRACTICES

E-1 INSPECTION OF SUPPLIES - FIXED PRICE, FAR 52.246-2 IAW 48.302

G110 CONTRACTOR REPORTING REQUIREMENTS AFLC FAR SUPP 52.212-9000 IAW 12.304(90)

H-41 CHANGES IN EXECUTIVE ORDER OR STATUTES, AFLC FAR SUPP 52.216-9012 IAW 16.703

I-61 REQUIRED SOURCES FOR JEWEL BEARINGS AND RELATED ITEMS, FAR 52.208-1

I-83 NEW MATERIALS, FAR 52.210-5

I-84 USED OR RECONDITIONED MATERIAL RESIDUAL INVENTORY AND FORMER GOVERNMENT SURPLUS PROPERTY, FAR 52.210-7

I-102 DEFENSE PRIORITY AND ALLOCATION REQUIREMENTS, FAR 52.212-8

I-228 UTILIZATION OF LABOR SURPLUS AREA CONCERNS, FAR 52.220-3

I-229 LABOR SURPLUS AREA SUBCONTRACTING PROGRAM, FAR 52.220-4

I-274 AFFIRMATIVE ACTION SPECIAL DISABLED AND VIETNAM ERA VETERANS, FAR 52.222-35

I-276 AFFIRMATIVE ACTION FOR HANDICAPPED WORKERS, FAR 52.222-36

I-278 EMPLOYMENT REPORTS ON SPECIAL DISABLED VETERANS AND VETERANS OF THE VIETNAM ERA, FAR 52.222-37

I-573 COMPETITION IN SUBCONTRACTING, FAR 52.244-5

IA-76 REQUIRED SOURCES FOR MINIATURE AND INSTRUMENT BALL BEARINGS, DFARS 252.208-7000

IA-77 REQUIRED SOURCES FOR PRECISION COMPONENTS FOR MECHANICAL TIME DEVICES, DFARS 252.208-7001

IA-79 REQUIRED SOURCES FOR HIGH CARBON FERROCHROME (FCH), DFARS 252.208-7003

IA-288 QUALIFYING COUNTRY SOURCES AS SUBCONTRACTORS, DFARS 252.225-7002

IA-292 DUTY FREE ENTRY QUALIFYING COUNTRY END PRODUCTS AND SUPPLIES, DFARS 252.225-7008

IA-294 PREFERENCE FOR DOMESTIC SPECIALTY METALS (MAJOR PROGRAMS), DFARS 252.225-7011

IA-295 PREFERENCE FOR DOMESTIC SPECIALTY METALS, DFARS 252.225-7012

IA-22 SPECIAL PROHIBITION ON EMPLOYMENT, DFARS 52.203-7001

IA-287 BUY AMERICAN ACT AND BALANCE OF PAYMENTS PROGRAM, DFARS 252.225-7001

IA-291 BUY AMERICAN ACT, TRADE AGREEMENT ACT AND THE BALANCE OF APYMENT PROGRAM, DFARS 252.225-7006

IA-306 RESTRICTION ON CONTRACTING WITH TOSHIBA OR KONGSBERG VAPENFABRIKK, DFARS 252.225-7027

H-41 CHANGES IN EXECUTIVE ORDER OR STATUTES, AFLC FAR SUPP 52.216-9012

I-83 NEW MATERIAL, FAR 52.210-5

I-84 USED OR RECONDITIONED MATERIAL RESIDUAL INVENTORY AND FORMER GOVERNMENT SURPLUS PROPERTY, FAR 52.210-7

IA-270 NOTICE OF RADIOACTIVE MATERIALS, DFARS 252.223-7000

IA-271 SAFETY PRECAUTIONS FOR AMMUNITION AND EXPLOSIVES, DFARS 252.223-7001

IA-272 CHANGE IN PLACE OF PERFORMANCE - AMMUNITION AND EXPLOSIVES, DFARS 252.223-7002

IA-298 LIMITATION OF SALES COMMISSIONS AND FEES FOR FOREIGN GOVERNMENTS, DFARS 252.225-7017

IV. DATA RIGHTS

E-1 INSPECTION OF SUPPLIES - FIXED PRICE, FAR 52.246-2

H-41 CHANGES IN EXECUTIVE ORDER OR STATUTES, AFLC FAR SUPP 52.216-9012

I-21 RESTRICTIONS ON SUBCONTRACTOR SALES TO THE GOVERNMENT, FAR 52.203-6

DETAILED CATEGORIZED LIST (BY TITLE)

Additional Clauses Found in an Earlier Version of the BOA Matrix but Excluded From the May 5, 1989 Version

I. FINANCE/AUDIT

PRICE REDUCTION FOR DEFECTIVE COST OR PRICING DATA, FAR 52.215-22

PRICE REDUCTION FOR DEFECTIVE COST OR PRICING DATA - MODS, FAR 52.215-23

SUBCONTRACTOR COST OR PRICING DATA, FAR 52.215-24

SUBCONTRACTOR COST OR PRICING DATA - MODS, FAR 52.215-25

COST ACCOUNTING STANDARDS, FAR 52.230-3

ADMINISTRATION OF COST ACCOUNTING STANDARDS, FAR 52.230-4

II. FLOWDOWN AND PRE-EXISTING COMMERCIAL SOURCE DECISIONS

PRICE REDUCTION FOR DEFECTIVE COST OR PRICING DATA, FAR 52.215-22

PRICE REDUCTION FOR DEFECTIVE COST OR PRICING DATA - MODS, FAR 52.215-23

SUBCONTRACTOR COST OR PRICING DATA, FAR 52.215-24

SUBCONTRACTOR COST OR PRICING DATA - MODS, FAR 52.215-25

COST ACCOUNTING STANDARDS, FAR 52.230-3

ADMINISTRATION OF COST ACCOUNTING STANDARDS, FAR 52.230-4

UTILIZATION OF SMALL BUSINESS CONCERNS AND SMALL DISADVANTAGED BUSINESS CONCERNS, FAR 52.219-8

SMALL BUSINESS AND SMALL DISADVANTAGED BUSINESS SUBCONTRACTING PLANS, FAR 52.219-9

CERTIFICATION OF NONSEGREGATED FACILITIES, FAR 52.222-21

EQUAL OPPORTUNITY, FAR 52.222-26

PREFERENCES FOR CERTAIN DOMESTIC COMMODITIES, DFARS 252.225-7009

PREFERENCE FOR PRIVATELY OWNED U.S.-FLAG COMMERCIAL VESSELS, FAR 52.247-64

III. STATUTORY AND/OR REGULATORY OVERLAP/INTERFERENCE WITH COMMERCIAL PRODUCTION PRACTICES

UTILIZATION OF SMALL BUSINESS CONCERNS AND SMALL DISADVANTAGED BUSINESS CONCERNS, FAR 52.219-8

SMALL BUSINESS AND SMALL DISADVANTAGED BUSINESS SUBCONTRACTING PLANS, FAR 52.219-9

PREFERENCES FOR CERTAIN DOMESTIC COMMODITIES, DFARS 252.225-7009

PREFERENCE FOR PRIVATELY OWNED U.S.-FLAG COMMERCIAL VESSELS, FAR 52.247-64

CLEAN AIR & WATER, FAR 52.223-1,-2

IV. TECHNICAL DATA RIGHTS

N/A

EXPLANATION OF CATEGORIES

NOT APPLICABLE (NOT APPLIC.):

These clauses are either self-deleting, unnecessary, or clearly incongruent with the purpose of this contract. Retaining them would indicate that we believe they do apply, and would represent sloppy contracting methodology.

REVISION REQUIRED (REV REQ'D):

These clauses require some kind of revision to make them accurate and/or acceptable. The revision required is indicated in the "Comments" column.

NO FLOWDOWN:

These are clauses with which The Boeing Company complies and which we will accept in our prime contracts. However, our commercial suppliers do not accept military terms and conditions in their purchase agreements. Accordingly, flowdown of these clauses into our subcontracts is not possible.

INCOMPATIBLE WITH COMMERCIAL PURCHASING SYSTEM (INCOMPT WITH COMM SYS):

These are clauses which are not compatible with a commercial purchasing system. Imposition of these clauses would be disruptive to our commercial suppliers and could be extremely expensive in other ways. Commercial buying procedures, as well as Boeing-Vendor relationships, would have to be changed (militarized). The items to be provided under this BOA will be sold to the Government on a market price basis, just as they are to any other customer.

NO SUBCONTRACTING OPPORTUNITIES (NO SUB CONTRCT OPPS):

No subcontracting opportunities exist because commercial decisions were made long before this, in a commercial spares situation.

UNACCEPTABLE CLAUSES MATRIX

SEQ #	TITLE AND F.A.R./D.F.A.R.S. REFERENCE	NOT APPLIC.	REV REQ'D	NO FLOW DOWN	INCOMPT WITH COMM SYS	NO SUB-CONTRCT OPPS	COMMENTS
B-900	SUPPLIES TO BE ORDERED		X				NEED APPROVAL OF BCA
~~E-1~~ DELETED FROM BOA	~~INSPECTION OF SUPPLIES FIXED~~ ~~PRICE,FAR 52.246.2,IAW 46.302~~				X		~~BCA COMPLIES WITH FAA REGS AND ON-~~ SHELF SUPPLIES ARE COMPLETED AT TIME OF ORDER, SO INPROCESS INSPECTION [redacted] NOT POSSIBLE
~~F-34~~ DELETED	~~F.O.B. ORIGIN W/ DIFFERENTIALS~~ ~~FAR 52.247.33,IAW 47.303-5(C)~~				X		~~WE NEVER WOULD USE THIS METHOD.~~ SHIPPING SAYS DELETE
F-53	MATERIAL IN SUPPORT OF FOREIGN MILITARY SALES. AFLC FAR SUP 52.247-9004, IAW AFLC FAR SUP 47.305-10(D)(91)	X					NOT IN MILITARY BOA. WE GET SHIPPING INSTRUCTIONS IN ORDERS (NOTE: WE DONT HAVE COPY OF CLAUSE)
~~F-69~~ DELETED	~~TRANSPORTATION TRANSIT PRIVILEGE~~ ~~CREDITS, FAR 52.247-57,~~ ~~IAW 47.305-13(B)(4)~~	X					~~DOES NOT APPLY TO BOEING (SEE ALSO K-25)~~
G110	CONTRACTOR REPORTING REQUIREMENTS AFLC FAR SUP 52.212-9000, IAW 12.304(90)				X		SEE I-102. DPAS IS STATUTORY BUT DOES NOT APPLY TO MATERIAL IN COMMERCIAL MARKETPLACE. FLOWDOWN IS REGULATORY AND CAN BE WAIVED
H-1	MATERIAL INSPECTION AND RECEIVING REPORT		X				DLA'S NEED TO BE ADDED TO PARAGRAPH (E) JUST AS IN BOA-7514
~~H-3~~ Deleted	~~VALUE ENGINEERING CHANGE PROPOSALS~~ ~~IAW FAR 48.103 (A) AND~~ ~~52.248-1(C)(D)~~	X					~~WE WOULD NOT HAVE ANY VECPS ON~~ CATALOG ITEMS (REQUIRES DEVIATION TO DELETE)

@=STATUTORY CLAUSE X=MAIN PROBLEM CATEGORY *=ALSO A PROBLEM TO THIS CATEGORY

UNACCEPTABLE CLAUSES MATRIX

SEQ #	TITLE AND F.A.R./D.A.R. REFERENCE	NOT APPLIC.	REV REQ'D	NO FLOW DOWN	INCOMPT WITH COMM SYS	NO SUB CONTRCT OPPS	COMMENTS
H-41	CHANGES IN EXECUTIVE ORDER OR STATUTES, AFLC FAR SUP 52.216-9012 IAW 16.703 (C)(71)				X		(NOTE: NEED COPY OF CLAUSE)
H-42	DESIGN CHANGES, AFLC FAR SUP 52.217-9026,IAW 17.7203-90 SAYS "INSERT CLAUSE IN FP CONTRACTS FOR ALL SPARE PARTS"	X					THERE WOULD BE NO DESIGN CHANGES APPROVED BY GOVERNMENT IN CATALOG ITEMS (NOTE: NEED COPY OF CLAUSE)
H-56	INCORPORATION OF SUBCONTRACTING PLAN, IAW FAR 19.705-5(A)(5)				X		REFERS TO PLAN FOR SMALL BUSINESS
H-78	AUDIT OF COMMERCIAL PRICES, AFLC FAR SUP 52.215-9010,IAW 15.892(B)				@		COMPANION TO K-70 CERTIFICATION. RESOLUTION BY USE OF CLAUSE FROM WICHITA BOA-6646
H-180	SUPPLIES TO BE ACCORDED DUTY FREE ENTRY, FAR SUP 252.225-7007, IAW 252.225-605				X		NOT REQUIRED OR DESIRED
STET ~~H-703~~	~~TYPES OF ORDERS~~		X				acceptable IN BOA
I-21	RESTRICTIONS ON SUBCONTRACTOR SALES TO THE GOVERNMENT,52.203-6			@			STATUTORY CLAUSE BUT FLOWDOWN IS REGULATORY
I-22	ANTI-KICKBACK PROCEDURES 52.203-7				@		STATUTORY CLAUSE AND FLOWDOWN
I-61	REQUIRED SOURCES FOR JEWEL BEARINGS AND RELATED ITEMS 52.208-1				★	X	SOURCING COMPLETED (SEE ALSO K-3)

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UNACCEPTABLE CLAUSES MATRIX

SEQ #	TITLE AND F.A.R./D.A.R. REFERENCE	NOT APPLIC.	REV REQ'D	NO FLOW DOWN	INCOMPT WITH COMM SYS	NO SUB CONTRCT OPPS	COMMENTS
I-83	NEW MATERIAL,52.210-5				X		CAN BE WAIVED BY PCO
I-84	USED OR RECONDITIONAL MATERIAL, RESIDUAL INVENTORY AND FORMER GOVERNMENT SURPLUS PROPERTY 52.210-7				X		CAN BE WAIVED BY PCO (SEE L-8)
I-102	DEFENSE PRIORITY AND ALLOCATION REQUIREMENTS 52.212-8				@		STATUTORY CLAUSE BUT FLOWDOWN IS REGULATORY (SEE L-7)
I-127	EXAMINATION OF RECORDS BY COMPTROLLER GENERAL 52.215-1				@		STATUTORY CLAUSE AND FLOWDOWN COULD BE ACCEPTED IF AUDIT IS RESTRICTED TO PRICE DATA, NOT COST DATA
I-128	AUDIT NEGOTIATION 52.215-2				@		STATUTORY CLAUSE. CLASS EXEMPTION FROM PROVIDING C&P DATA WOULD MAKE THIS NOT APPLICABLE
I-144	ORDER OF PRECEDENCE 52.215-33		X				DELETE SECTIONS L AND M FROM PRECEDENCE OR MAKE LAST
I-214	UTILIZATION OF SMALL BUSINESS CONCERNS AND SMALL DISADVANTAGED BUSINESS CONCERNS 52.219-8					@	STATUTORY CLAUSE AND FLOWDOWN. SHOULD BE N/A TO PRIME CONTRACT; BUT IF WE ACCEPT, CANNOT FLOWDOWN (SEE ALSO K-41AND L-118)
I-215	SMALL BUSINESS AND SMALL DISADVANTAGED BUSINESS SUBCONTRACTING PLAN					@	STATUTORY CLAUSE SAME AS ABOVE (SEE L-123)

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UNACCEPTABLE CLAUSES MATRIX

SEQ #	TITLE AND F.A.R./D.A.R. REFERENCE	NOT APPLIC.	REV REQ'D	NO FLOW DOWN	INCOMPT WITH COMM SYS	NO SUB CONTRCT OPPS	COMMENTS
I-228	UTILIZATION OF LABOR SURPLUS AREA CONCERNS, 52.220-3					@	STATUTORY CLAUSE BUT FLOWDOWN REGULATORY-CAN BE WAIVED BY SECRETARY OF LABOR (SEE ALSO K-39)
I-229	LABOR SURPLUS AREA SUBCONTRACTING PROGRAM 52.220-4					@	STATUTORY CLAUSE SAME AS ABOVE
I-267	EQUAL OPPORTUNITY PREAWARD CLEARANCE OF SUBCONTACTS, 52.222-28				@	★	STATUTORY CLAUSE WE COMPLY AND INCLUDE EQ.OP. INSUBS, BUT WON'T WAIT FOR ACO TO LET CONTRACTS. WAIVER AVAILABLE FROM OFCCP
~~I-268~~	~~NOTIFICATION OF VISA DENIAL 52.222-29~~	X					
I-274	AFFIRMATIVE ACTION FOR SPECIAL DISABLED AND VIETNAM ERA VETERANS 52.222-35			@			STATUTORY CLAUSE AND FLOWDOWN. WAIVER AVAILABLE FROM OFCCP
I-276	AFFIRMATIVE ACTION FOR HANDICAPPED WORKERS, 52.222-36			@			STATUTORY CLAUSE AND FLOWDOWN. SAME AS ABOVE
I-278	EMPLOYMENT REPORTS ON SPECIAL DISABLED VETERANS AND VETERANS OF THE VIETNAM ERA					@	PRIME CONTRACT WAIVER REQUIRED STATUTORY CLAUSE AND FLOWDOWN SAME AS ABOVE
I-292	CLEAN AIR AND WATER 52.223-2			@			STATUTORY CLAUSE WE COMPLY, SUBS COMPLY WITH PUBLIC (ENVIRONMENTAL) LAWS (SEE ALSO K-19 TO BE REVISED)

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UNACCEPTABLE CLAUSES MATRIX

SEQ #	TITLE AND F.A.R./D.A.R. REFERENCE	NOT APPLIC.	REV REQ'D	NO FLOW DOWN	INCOMPT WITH COMM SYS	NO SUB CONTRCT OPPS	COMMENTS
I-293	HAZARDOUS MATERIAL IDENTIFICATION AND MATERIAL SAFETY DATA 52.223-3		X				REPLACE WITH AF FAR SUP 52.223-9000 "WAIVER OF....." (SEE ALSO K-53)
I-311	DUTY FREE ENTRY 52.225-10				✱	X	PRICE IS SAME, WITH OR WITHOUT DUTY TOO MUCH PAPERWORK TO ACCEPT
I-317	NOTICE AND ASSISTANCE REGARDING PATENT AND COPYRIGHT INFRINGEMENTS 52.227-2				X		MORE TROUBLE THAN IT'S WORTH
I-318	PATENT INDEMNITY 52.227-3				X		SAME AS ABOVE
I-352	FEDERAL, STATE AND LOCAL TAXES 52.229-3				X		
I-353	FEDERAL, STATE AND LOCAL TAXES 52.229-4				X		CATALOG PRICES DO NOT CONTAIN CONTINGENCY FOR TAXES AND WILL NOT CHANGE CONTRACT PRICE
I-354	TAXES CONTRACTS PERFORMED IN U.S. POSSESIONS OR PUERTO RICO 52.229-5				X		NO PERFORMANCE OUTSIDE OF WASHINGTON STATE
I-391	DISCOUNTS FOR PROMPT PAYMENT 52.232-8				X		NONE OFFERED
~~I-418~~	~~DISPUTES ALTERNATE 1, 52.233-1~~	~~X~~					

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UNACCEPTABLE CLAUSES MATRIX

SEQ #	TITLE AND F.A.R./D.A.R. REFERENCE	NOT APPLIC.	REV REQ'D	NO FLOW DOWN	INCOMPT WITH COMM SYS	NO SUB CONTRCT OPPS	COMMENTS
I-419	PROTEST AFTER AWARD 52.233-3	X					acceptable
I-546	CHANGES FIXED PRICE 52.243-1	X					
I-568	SUBCONTRACTS (FP CONTRACTS) 52.244-1	X			★		DOES NOT APPLY TO FFP CONTRACTS PER PARAGRAPH (A) OF FAR CLAUSE
I-573	COMPETITION IN SUBCONTRACTING 52.244-5	★			★	X	PRICES ARE SET BY CATALOG. WE PROBABLY COMPLY WITH THIS CLAUSE
~~I-602~~	~~PREFERENCE FOR U.S. FLAG AIR CARRIERS, 52.247-63~~				X	★	~~NO GOVERNMENT FUNDS UTILIZED FOR AIR~~ TRANSPORTATION; WE WOULD NEVER KNOW FOR ON-THE-SHELF ITEMS
IA-22	SPECIAL PROHIBITION ON EMPLOYMENT 252.203-7001			@			STATUTORY CLAUSE BUT FLOWDOWN IS REGULATORY
IA-24	DISPLAY OF DoD HOTLINE POSTER 252.203-7003			@			? STATUTORY FLOWDOWN NOT REQUIRED BOEING COMPLIES
IA-76	REQUIRED SOURCES FOR MINIATURE AND INSTRUMENT BALL BEARINGS 252.208-7000				★	X	SEE ALSO K-50
IA-77	REQUIRED SOURCES FOR PRECISION COMPONENTS FOR MECHANICAL TIME DEVICES 252.208-7001				★	X	SEE ALSO K-49

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UNACCEPTABLE CLAUSES MATRIX

SEQ #	TITLE AND F.A.R./D.A.R. REFERENCE	NOT APPLIC.	REV REQ'D	NO FLOW DOWN	INCOMPT WITH COMM SYS	NO SUB CONTRCT OPPS	COMMENTS
~~IA-78~~	~~REQUIRED SOURCES FOR HIGH PURITY SILICON 252.208-7002~~				~~★~~	~~X~~	~~SEE ALSO K-51~~
IA-79	REQUIRED SORUCES FOR HIGH CARBON FERROCHROME, 252.208-7003				★	X	SEE ALSO K-47
~~IA-82~~	~~REQUIRED SOURCES FOR ANTI FRICTION BEARINGS 252.208-7006~~				~~★~~	~~X~~	
IA-90	ACQUISTIONS FROM DEFENSE CONTRACTOR SUBJECT TO ON SITE INSPECTION UNDER INF TREATY 252.209-7001	X					CANNOT ACCEPT BECAUSE HAVE NOT BEEN ABLE TO GET A COPY OF THE CLAUSE
IA-225	SMALL DISADVANTAGED BUSINESS SUBCONTRACTING PLAN 252.219-7000					@	STATUTORY (SEE I-215)
IA-232	INCENTIVE PROGRAM FOR SUBCONTRACTING WITH SMALL AND DISADVANTAGED BUSINESS CONCERNS, BLACK COLLEGES AND UNIVERSITIES, AND MINORITY INSTITUTIONS 252.219-7009					X	SEE I-215
IA-270	NOTICE OF RADIOACTIVE MATERIALS 252.223.7000	X					WE HAVE NONE
IA-271	SAFETY PRECAUTIONS FOR AMMUNITION AND EXPLOSIVES	X					MAY NEED THESE DUE TO PROPELLANTS?

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UNACCEPTABLE CLAUSES MATRIX

SEQ #	TITLE AND F.A.R./D.A.R. REFERENCE	NOT APPLIC.	REV REQ'D	NO FLOW DOWN	INCOMPT WITH COMM SYS	NO SUB CONTRCT OPPS	COMMENTS
IA-272	CHANGE IN PLACE OF PERFORMANCE AMMUNITION AND EXPLOSIVES 252.223-7002	X					MAY NEED THESE DUE TO PROPELLANTS?
IA-287	BUY AMERICAN ACT AND BALANCE OF PAYMENTS PROGRAM 252.225-7001	@			★	★	STATUTORY FAR CLAUSE 25.108 (D)(1) LISTS CERTAIN ARTICLES THAT ARE CONSIDERED NOT TO BE MANUFACTURED IN THE U.S. IN SUFFICIENT QUANTITIES. LIST INCLUDES "SPARE AND REPLACEMENT PARTS FOR EQUIPMENT OF FOREIGN MANUFACTURE AND FOR WHICH DOMESTIC PARTS ARE NOT AVAILABLE". SOURCES ALREADY DETERMINED (SEE ALSO K-37)
IA-288	QUALIFYING COUNTRY SOURCES AS SUBCONTRACTORS 252.225-7002				★	X	
IA-291	BUY AMERICAN ACT, TRADE AGREEMENT ACT AND THE BALANCE OF PAYMENTS PROGRAM 252.225-7006				★	@	CAN BE USED IN LIEU OF IA-287 ABOVE. (SEE ALSO K-38) THEREFORE CAN BE DELETED JUST LIKE IA-287
IA-292	DUTY FREE ENTRY QUALIFYING COUNTRY END PRODUCTS AND SUPPLIES 252.225-7008				★	X	SEE I-311 COMMENT
~~IA-293~~	~~PREFERENCE FOR CERTAIN DOMESTIC COMMODITIES 252.225-7009~~	★			@	★	~~25.7002(A)(6) APPLIES AS ONLY SEATS~~ HAVE FABRIC AND VALUE IS LESS THAN 10% OF COST OF THE SEAT

Page 8 @=STATUTORY CLAUSE X=MAIN PROBLEM CATEGORY ★ ALSO A PROBLEM TO THIS CATEGORY

UNACCEPTABLE CLAUSES MATRIX

SEQ #	TITLE AND F.A.R./D.A.R. REFERENCE	NOT APPLIC.	REV REQ'D	NO FLOW DOWN	INCOMPT WITH COMM SYS	NO SUB CONTRCT OPPS	COMMENTS
IA-294	PREFERENCE FOR DOMESTIC SPECIALTY METALS (MAJOR PROGRAMS) 252.225-7011	@					SPARES IS NOT A "PROGRAM" PER 25.7002 (D)(1). IA-295 IS APPROPRIATE CLAUSE
IA-295	PREFEREN[illegible] FOR DOMESTIC SPECIALTY METALS [illegible]52.225-7012				@	★	WAIVE PER PARAGRAPH (A)(i) AND/OR (ii) OF DFAR CLAUSE
IA-296C	DUTY FREE ENTRY ADDITIONAL PROVISIONS				★	X	SEE I-311 COMMENT
~~IA-297~~	~~U.S. PRODUCTS (MILITARY ASSISTANCE PROGRAMS)~~				~~X~~	~~★~~	~~SOURCING DECISIONS MADE PREVIOUSLY~~ (SEE ALSO K-58)
IA-298	LIMITATION ON SALES COMMISSIONS AND FEES FOR FOREIGN GOVERNMENTS	X				★	DOES NOT FIT SPARES SITUATION
IA-300	EXCLUSIONARY POLICIES AND PRACTICES OF FOREIGN GOVERNMENTS	X				★	DOES NOT APPLY TO SPARES SITUATION
IA-306	RESTRICTION ON CONTRACTING WITH TOSHIBA CORP. OR KONGSBERG VAPENFABRIKK 252.2225-7027					@	CAN BE WAIVED (SEE ALSO K-42)
~~IA-399~~	~~SUPPLEMENTAL COST PRINCIPLES~~	~~X~~					~~CAS NOT APPLICABLE, FY '87 ONLY (SEE ALSO~~ K-24)(SEE L-129C)
~~IA-448~~	~~RECOVERY OF NONRECURRING COSTS~~ ON COMMERCIAL SALES	~~X~~					~~THIS IS NOT RDT&E OR A PRODUCTION~~ CONTRACT. WE SHOULD HAVE THE REVERSE (RECOVERY OF COSTS ON MILITARY SALES)

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UNACCEPTABLE CLAUSES MATRIX

SEQ #	TITLE AND F.A.R./D.A.R. REFERENCE	NOT APPLIC.	REV REQ'D	NO FLOW DOWN	INCOMPT WITH COMM SYS	NO SUB CONTRCT OPPS	COMMENTS
IA-648	PRICING OF ADJUSTMENTS 252.243-7001	X					APPLIES TO CHANGES
K-52	SALES HISTORY				X		NOT ACCEPTABLE
K-70	CERTIFICATION OF COMMERCIAL PRICING 52.215-9009				X		NOT ACCEPTABLE - USE WICHITA BOA AGREEMENT
~~K-54~~	~~ROYALTY INFORMATION~~	~~X~~					~~IAW FAR 27.204-2 ONLY REQUIRED WHEN"~~
c ~~L-135~~	~~VERIFICATION OF SECURITY CLEARANCE~~	~~X~~					~~NO DD254 IN ANY ORDER~~
~~L-182~~	~~SAFETY PROGRAM PLAN~~	~~X~~					~~"REQUIREDFOR PROTECTION OF GFP"~~ NO GFP ON COMMERCIAL ITEMS

@=STATUTORY CLAUSE X=MAIN PROBLEM CATEGORY *=ALSO A PROBLEM TO THIS CATEGORY

MEMORANDUM

TO: Peter Levine
Senate Subcommittee on Oversight of Government Management

FROM: Naomi Williamson
Honeywell Inc., Business and Commuter Aviation Systems Division

DATE: 28 June 1989

SUBJ: **REGULATORY IMPEDIMENTS TO GOVERNMENT PROCUREMENT OF COMMERCIAL PRODUCTS IN ADDITION TO COST OR PRICING DATA/AUDIT.**

We are providing this Memorandum as a supplement to the Honeywell testimony given to your Subcommittee on 16 May 1989 where Honeywell appeared as one of the representatives of the Electronic Industries Association. As a commercial division of Honeywell, we firmly support a change in regulatory approach by the DOD in dealing with commercial products and contractors. Specifically, rather than trying to carve out a few exceptions to cost or pricing data, certification and audit regulations, the best approach would be to carve out or create a minimum set of regulations that do apply to government contracts with commercial vendors. The system must not operate by exception. It must be easy to understand by both commercial contractors and government procurement officers. This will best alleviate the disincentives and barriers commercial contractors face when attempting to sell commercial products to the government. This memorandum addresses the categories of regulatory requirements that create impediments to commercial contractors doing business with the government or government primes in addition to the cost or pricing data issues.

SUMMARY

Essentially, any Government Regulation that requires or may require a commercial contractor to change its current practices for producing the commercial product the Government wishes to buy can create a barrier. These barriers, in addition to cost or pricing data issues, fall into the general areas of: regulations that require implementation of or changes to procedures not required by the commercial market; regulations that require reports not necessary in the normal course of business; regulations affecting subcontracts with our vendors; regulations that open the door to audit and hence control by government inspectors of the commercial production line; regulations that jeopardize the commercial contractor's ownership of commercially developed designs.

DCASR OR DCASM AUDIT RIGHTS

Example: FAR 52.246-2 - CONTRACTOR INSPECTION REQUIREMENTS

This regulation grants the Government the right to inspect "supplies" including "raw material, components, intermediate assemblies, end products, and lots of supplies" on the contractor's premises and requires flow-down to subcontractors. Commercial assembly lines build both Government and commercial product simultaneously and do not designate which will be allocated to the Government until the end product is ready to ship. This regulation gives the Government the right to disrupt the production line for products going to commercial customers and to inspect sub-assemblies and potentially suppliers. It also requires the "Contractor to provide and maintain in inspection system acceptable to the Government...." along with facilities for the Government inspector to use. This creates the potential for increased cost and change based not on the commercial contractor or market's judgment of what is required, but opens the contractor to risk that any Government inspector could declare that working, in-place systems must be changed.

TECHNICAL DATA RIGHTS

Examples: DFAR 52.227.7018 *et seq* - RIGHTS IN TECHNICAL DATA AND COMPUTER SOFTWARE; 52.248-1 - VALUE ENGINEERING

These regulations require the contractor to adopt the very strict Government methods for marking technical data if the contractor's proprietary designs and other technical data is to be protected from government appropriation or distribution. Most commercial contractors are not familiar with the Government requirements and do not use the government system for marking. They have systems in place that have worked adequately for years in the commercial marketplace. Since the engineers who work on the commercial programs are not sensitized to the risks associated with giving the government data, a commercial contractor faces the risk of inadvertently giving away contractor funded designs.

Further, where the Government pays for a modification to a commercial product, the commercial contractor faces the risk of losing the rights to the basic design or the inconvenience and expense of segregating each part of the design specifically created for the modification and providing an essentially useless piece of technical data to the Government to satisfy the regulation.

In addition, commercial contractor format may not conform to Government practices.

Value engineering brings up a number of issues in addition to ownership of designs value engineered. The most important is that the existing commercial product is being changed which may create a unique product bought only by the Government (not sold in the commercial marketplace).

REGULATIONS AFFECTING SOURCES

Examples: 52.208-1 - REQUIRED SOURCES FOR JEWEL BEARINGS...; 52.219-13 - UTILIZATION OF WOMEN OWNED BUSINESSES; 52.220-3 - UTILIZATION OF LABOR SURPLUS AREA CONCERNS; 52.219-8 - UTILIZATION OF SMALL BUSINESS CONCERNS; 52.203-7001 - SPECIAL PROHIBITION ON EMPLOYMENT; 52.204-7005 - OVERSEAS DISTRIBUTION OF DEFENSE SUBCONTRACTS

The advantage to the Government of purchasing of commercial products is that the basic product has been designed without the Government funding the effort--and the product is available in the commercial marketplace. This necessitates the selection of sources before the Government ever gets interested in buying the product. In this context, regulations controlling the sourcing of subcontracts do not make sense. The commercial contractor's objection to accepting these provisions has nothing to do with whether the company endorses the policy promoted by the regulation. In order to comply, they must investigate and report on whether they are already in compliance or they must terminate substantial subcontracts, pay penalties and risk jeopardizing the commercial production line for the usually small quantity Government buys. In some cases, extremely sophisticated equipment that does not lend itself well to the small or disadvantaged business concern.

CHANGES IN PROCEDURES/REPORTING REQUIREMENTS

Examples: 52.203-7 - ANTIKICKBACK PROCEDURES; 52.225-7008 - DUTY FREE ENTRY; 52.217-12 - PATENT RIGHTS; 52.219-9 - SMALL BUSINESS PLAN; 52.220-4 - LABOR SURPLUS AREA PLAN

This type of regulation requires the contractor to hire additional staff to track data and create reports for the Government. Such reports do not need to be created for the commercial marketplace and become a cost of doing business caused by the Government but paid for by all purchasers of our products. That may not sound bad, but where price in a market competition is a matter of business life and death, such requirements can be sufficient for a commercial contractor to decide it is not worth it to accept a Government order that includes these requirements. Commercial contractors do not employ the staffs to create such reports and host the audits should the Government decide to check up on the reports.

CONCLUSION

Creating exception procedures to the current body of regulations that can or may apply to all contracts with the government would be inadequate for eliminating the barriers that keep commercial contractors from competing for government contracts. Solving the cost or pricing data issue alone will do nothing to provide guidance to contracting officers who must negotiate contracts with commercial contractors that include, at a minimum, the above issues also created by the regulations.

Requiring commercial contractor's to wade through the plethora of Government regulations they do not employ the staffs to understand and may not comply with is not the answer--especially when the penalties for failure to comply are criminal.

FOOTNOTE

As a follow-up to the LRAACA example that was given at the 16 May hearing, Lockheed asked Honeywell BCASD to continue to consider supplying two subsystems for the Navy that require no modification to fit the Navy application (truly NDI). In order to assure continued availability of product for their production line, they must negotiate a complete contract that addresses the above issues. The two subsystems are relatively inexpensive; therefore, the dollar value of the subcontract provides little incentive for Honeywell to take any risks when it comes to imposition of regulatory requirements that drive up costs or require us to change our way of doing business.

Aerospace
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A. S. TVEIT

AP P&F 89-37
March 1, 1989

AEROSPACE PROCUREMENT SERVICE MEMORANDUM

TO: Procurement Techniques Committee

SUBJECT: Update of Unauthorized Clause Compendium

At the January meeting, the Procurement Techniques Committee decided to update the "Compendium of Unauthorized Policies and Clauses". The Compendium (attachment 1) was prepared in December 1987 to illustrate the unauthorized clause problem to Dr. Costello. The following list contains those unauthorized policies and clauses which have been identified since we prepared the compendium. Committee members responsible for initiating committee action on each clause or policy are asked to fill out the AIA Information Sheet (attachment 2). Once this information is obtained the Compendium will be revised and distributed to the committee.

Unauthorized Clauses & Policies Identified Since January 1988

Clause/Policy	Committee Member
1. AFLC "Hostilities Clause" This clause was withdrawn by AFLC following discussions with the Air Force.	Jim Williams
2. Naval Air Development Center Clauses - "Interpretation of Contract: Notice of Ambiguities" Clause - "Notice of Constructive Change" Clause These clauses were distributed to Procurement Techniques Committee members prior to May 1988 meeting. No other companies expressed concern.	Charles Rumbaugh
3. AFSC/CMD Policy on Approval for Purchases of Special Tooling & Test Equipment Latest revised language distributed to members at January 1989 meeting. Comments were to go to Omer Ruiz.	Omer Ruiz
4. AFCMD Regulation 540-10, Major Waiver and Deviation Policy	Jay Shiba

Clause/Policy	Committee Memeber
5. Organizational Conflict of Interest (OCI) Clauses (see AP P&F 88-281)	Kathy Hammock
6. DISC Clause A-200, Manufacturer's Identification Symbol Listing Requirement Distributed to members prior to October 1988 meeting. No other companies expressed concern.	Charles Rumbaugh
7. Revised S.F.1411 AIA/CODSIA letter to Duncan Holaday requesting the form be rescinded due to failure to obtain OMB paperwork clearances. (AP P&F 88-180). OMB has sided with industry (AP P&F 88-193 and AP P&F 88-210).	Jack Haggarty
8. Different Clauses Implementing MIL-STD 1567A, Work Measurement Members were to report any problems encountered to Walker Grubb at October 1988 meeting.	Walker Grubb
9. CECOM "Certificate of Performance" Clauses (AP P&F 88-271) A letter requesting that this clause be rescinded was sent to CECOM by EIA. Request was rejected. Clause is on agenda for discussion at Army meeting.	John Conners
10. USAF Space Division FAR Supplement Clause "Space, Human Assurance and Reliability Program (SHARP)"	Bill Fulton
11. SDIO Clause, "Safeguarding of Government Information"	Alan Chvotkin
12. Total Quality Management (TQM) Clauses e.g., Warner Robbins ALC SOW Provision	Alan Chvotkin/Arvid Tveit

Several new clauses which will be addressed for the first time at the San Diego meeting have not been included on this list. Please send your responses to Pat Sullivan at AIA by March 21, 1989.

Chuck

Chuck Cruit
Director, Contract Policies

Attachments

cc: Procurement & Finance Executive Group

(0112K/8)

Attachment 1

Compendium of Unauthorized Policies & Clauses

	Military Department/Component	Unauthorized Item (Clause/Policy Document)	Regulatory Violation/ Duplication	Issues	Current Status
1.	Ogden Air Logistics Center Hill Air Force Base	"Forbearance" Clause (OO-ALC FAR SUP 52.249.49-9001)	FAR 1.302, FAR/DFARS 1.304, FAR Subpart 12.2, FAR 52.249-9 and 52.212-4	• Unilateral imposition of clause providing for the equivalent of liquidated damages. • Clause inconsistent with FAR. • Ogden continues to pursue even though AFLC has instructed withdrawal of clause.	Clause ordered withdrawn by AFLC, but still in use.
2.	Air Force Logistics Command, Wright-Patterson	"Consequential Damages" Clause (AFLC FAR SUP 49.402-7, clause 52.249-9000, and Policy Letter 87-3)	FAR 1.302, FAR/DFARS 1.304, FAR Subpart 12.2, FAR 52.212-4, FAR 52.249-8	• Unilateral imposition of clause providing for the equivalent of liquidated damages. • Clause inconsistent with FAR.	Clause withdrawn by AFLC.
3.	Naval Air Systems Command	"Progress Payments-Withholding or Suspension-Ceiling Priced Orders" Clause (NAVAIR 52.217-9500) and "Additional Requirements Concerning the Changes Clause" clause ("H-23")	FAR 1.302, FAR 1.4, FAR 1.5, FAR/DFARS 1.304, and FAR 52.243-1 thru 52.243-4	• Clauses would automatically significantly limit progress payments below the standard FAR amounts prior to definitization of ceiling priced orders. • Overreaches recent Congressional legislation concerning unpriced orders. • Inconsistent with FAR and DFARS.	Clause is in use.
4.	DAR Council/Air Force Aeronautical Systems Division	DAR Council memorandum of 1/27/87 (DAR Case 85-2230, "Reimbursement, Interest Charges, and Penalties for Overpayment") and ASD "Reimbursement, Interest Charges, and Penalties for Overpayment" clause	10 U.S.C. 2306a (e), FAR 1.301(b), and FAR 1.5	• Failure to obtain public comment • Clause uses incorrect interest rate.	Clause is in use.

Military Department/Component	Unauthorized Item (Clause/Policy Document)	Regulatory Violation/ Duplication	Issues	Current Status
5. DAR Council	DFARS Appendix I change requiring unit prices on all DD Form 250s	FAR 1.5, statutes including Regulatory Flexibility Act and Paperwork Reduction Act	• Requires unit prices on all DD Form 250's for each item delivered. • Policy withdrawn after industry pointed out that not all contract prices are negotiated at the unit price level and that providing a copy of the contract to Government personnel seeking such information would be significantly less expensive.	DFARS Appendix I to be revised to delete mandatory requirement (DAC 86-6).
6. Air Force Electronic Systems Division	Contracting Policy Letter 85-12 ("Executive Estimate of Cost at Completion" clause)	FAR 1.301(b), FAR 1.302, FAR/DFARS 1.4 and FAR/DFARS 1.304	• Lack of public comment. • Improper use in fixed-price contracts.	Policy revised, but clause still in use.
7. Navy, Assistant Secretary for Shipbuilding and Logistics	Navy Policy Letter on Warranties, 9/8/86	FAR 1.302, FAR/DFARS 1.304, FAR 31.205-39, FAR/DFARS 46.7	• Not in conformance with FAR or DFARS. • Policy does not recognize, there may be a cost to the government associated with the acceptance of certain warranty provisions.	Policy not rescinded.
8. Navy, Assistant Secretary for Shipbuilding and Logistics	"Refunds (Spares and Support Equip.)(12/86)" Clause (NAVY FAR SUP 52.242-9000)	FAR 1.302, FAR/DFARS 1.304, Refund Policy memo from Secretary Weinberger on November 1, 1985	• Conflicts with the DoD-wide approach and provides for unilateral price redetermination and for refund negotiations on demand, two requirements that are fundamentally in opposition to sound contracting principles and practices.	Policy not rescinded.

Military Department/Component	Unauthorized Item (Clause/Policy Document)	Regulatory Violation/ Duplication	Issues	Current Status
9. Army Missile Command, Redstone Arsenal	Army Redstone Arsenal Policy Memorandum on the Use of CPFF Contracts, 11/11/85	FAR 15.9 and FAR 16.1	• Policy did not allow fees in excess of 6.5%. • Violation of DoD profit policy.	Policy revised.
10. Air Force Systems Command	"Contractor Standards for Controlling Restrictive Markings" (AFSC FAR Supp. 52.227-9002)	FAR 1.301(b), FAR 1.302, FAR/DFARS 1.304, FAR/DFARS 1.4, DFARS 52.227-7013; DFARS 52.227-7018	• Violates FAR/DFARS policy. • Lack of public comment. • Lack of a deviation.	Clause is in use.
11. Department of the Navy	SECNAV Instruction 4210.6, 20 November 1985 (Special tooling and test equipment, fixed-price development contracts)	DoDD 5000.1, FAR 1.301(b) FAR 1.5, FAR 16.1	• Promotes inappropriate use of fixed-price R&D contracts. • DoD has not supported requiring contractors to routinely make significant investment in special tooling and test equipment. • Navy has initiated the policy requiring contractors to invest as much as 100% of the production special tooling and test equipment. • Navy has openly supported present and proposed legislation notwithstanding stated DoD preference.	Navy policy not revised.
12. DCAA	"Overfunded Pension Plan" Clause/Advance Agreements.	FAR 1.301(a), FAR 1.302, FAR/DFARS 1.304, FAR /DFARS 1.4	• Lack of Public Comment. • Lack of FAR/DFARS deviation • DCAA is not authorized by the FAR to issue uniform contract clauses • Failure to demonstrate that supplemental coverage is needed to satisfy the specific needs of the agency.	Clause language proposed by DCAA is being used in advance agreements pending action by the DAR Council.

Military Department/Component	Unauthorized Item (Clause/Policy Document)	Regulatory Violation/ Duplication	Issues	Current Status
13. Air Force Systems Command	"Straight Arrow Program (APR 1986)," AFSC FAR SUPP 52.203-9000	FAR 1.301(b) FAR 1.302, FAR 1.5	• Lack of public comment. • Failure to demonstrate that supplemental coverage is needed to implement the FAR/DFARS or satisfy the specific needs of the agency.	Clause is in use.
14. U.S. Army Strategic Command	"Innovations" Clause	FAR 1.302, FAR 52.227-12, and FAR 27.303	• Failure to demonstrate that supplemental coverage is needed to implement the FAR/DFARS or satisfy the specific needs of the agency.	Clause is in use.
15. Joint Logistics Commanders	Data Rights Policies and Clauses, AFSC/AFLC 800-16	FAR 1.301(b), FAR 1.302, FAR/DFARS 1.304, FAR 1.5, FAR 52.227-7018	• Lack of public comment. • Issued outside of FAR system. • Improper supplementation of FAR/DFARS.	Clauses is in use.
16. Air Force Systems Command	"Total System Performance Responsibility (APR 1987)", (AFSC FAR SUPP 52.217-9001)	FAR 1.301(b), FAR 1.302, FAR/DFARS 1.304, FAR/DFARS 1.4, FAR 1.5 FAR 52.245-2,	• Clause is inconsistent w/rights recognized under ASBCA cases in the area of constructive changes, defective specs., etc. • Lack of FAR/DFARS deviation. • Lack of public comment. • Clause is inconsistent w/FAR. • Failure to demonstrate that supplemental coverage is needed to implement the FAR/DFARS or satisfy the specific needs of the agency.	Clause is in use.

Military Department/Component	Unauthorized Item (Clause/Policy Document)	Regulatory Violation/ Duplication	Issues	Current Status
17. Navy Strategic Systems Project Office	"Complete and Final Equitable Adjustments" Clause	FAR 1.302, FAR/DFARS 1.4	• Clause constitutes deviation from the standard DFARS settlement language. • Provides for automatic waiver of contractor's right to an equitable adjustment under any other clause if the claim is based on the change order's impact on that clause. • Lack of a deviation.	Clause is in use.
18. Navy Strategic Systems Project Office	"DoD FAR Supplement" Clause	FAR 1.302, FAR/DFARS 1.304, FAR/DFARS 1.4	• Clause states that all references to FAR also include corresponding DFARS and that in the event of a conflict between the two, the DFARS control. • Lack of a deviation.	Clause is in use.
19. Naval Air Systems Command	"Orders-Fixed Price (June 1987)" Clause (NAVAIR 52.216-9534)	P.L. 99-500, section 908, FAR/DFARS 1.304, FAR/DFARS 1.4, Interim Rule - DFARS 217.75	• Lack of a deviation. • Improper supplementation of DFARS. • No attempt to limit the contractor's expenditures or obligations to equate to the government's obligations of 50% or 75% of the ceiling price for unpriced contract actions as required by statute and the DoD Interim Rule.	Clause is in use.
20. Military Departments	Data Rights Clauses	FAR 1.302, FAR/DFARS 1.304, FAR/DFARS 1.4	• Military services continue to use a variety of data rights clauses even though the deviation that authorized them was rescinded on December 30, 1985.	Clauses in use.

D. ADDITIONAL MATERIALS PROVIDED BY THE DEPARTMENT OF DEFENSE

INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202

REPORT
No. 87-214

August 7, 1987

MEMORANDUM FOR ASSISTANT SECRETARY OF THE ARMY (FINANCIAL MANAGEMENT)
ASSISTANT SECRETARY OF THE NAVY (FINANCIAL MANAGEMENT)
COMPTROLLER OF THE AIR FORCE
DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Final Report on the Survey of the Military Departments' and Defense Agencies' Implementation of the Federal Acquisition Regulation (Project No. 7CC-003)

Introduction

This is our final report on the survey of the Military Departments' and the Defense agencies' implementation of the Federal Acquisition Regulation. This audit was a follow-on to the audit of "DoD's Implementation of the Federal Acquisition Regulation," Report No. 87-072, January 28, 1987. The objective of the audit was to determine if the Military Departments' and the Defense agencies' supplements to the Federal Acquisition Regulation (Service supplements) were prepared in accordance with the criteria established in the Federal Acquisition Regulation. We had planned a comprehensive audit of each of the supplements. However, we concluded our effort at the end of the survey with this report. We plan to review each of the Service supplements in the future after the problems identified are corrected and the actions recommended are taken.

Scope of Survey

The survey was conducted at offices of the Military Departments, including major commands, Defense agencies, and their primary-level field activities that prepared the respective supplements to the Federal Acquisition Regulation. We interviewed appropriate officials to determine whether the guidance given and the procedures used to prepare the original supplements issued during 1984 were adequate. Also, we examined the procedures used to review and approve changes to the supplements or for the development of new supplements. To determine compliance with the Federal Acquisition Regulation, we reviewed a random sample of sections from supplements issued by the Army, Navy, Air Force, and Defense Logistics Agency. Where applicable, the coverage in these supplements was compared to the

ENCLOSURES

coverage in the Defense supplement and the Federal Acquisition Regulation.[1]

We did not include the Defense Mapping Agency's supplement in the conclusions reached in survey because the supplement was less than 20 pages in length. Neither the Defense Nuclear Agency nor the Defense Communications Agency issued supplements to the Federal Acquisition Regulation. This compliance survey was conducted from October through November 1986 in accordance with generally accepted government auditing standards. Enclosure 2 is a list of activities visited.

Background

In Report No. 87-072, we reported that approximately 20 percent of the coverage in the Defense supplement did not meet the Federal Acquisition Regulation criteria for preparing a supplement. The short time frame the developers had to prepare the Defense supplement was the cause of this condition. However, we commended the developers for the minimal, 27 lines, inconsistent coverage. We recommended that the Director of the Defense Acquisition Regulatory Council eliminate duplicative and unnecessary coverage and make appropriate changes to the Defense supplement using our line-by-line analysis as a guide. We also recommended that the Director establish and implement formal procedures to review all new acquisition regulatory provisions first for inclusion in the Federal Acquisition Regulation, and then in the Defense supplement. The Assistant Secretary of Defense for Production and Logistics (formerly Acquisition and Logistics) concurred with our recommendations and has instituted the proper review procedures.

Federal Acquisition Regulation 1.301(a)(2) allows the Secretary of Defense to authorize supplements to the regulation at any organizational level. The criteria that the Military Departments and Defense agencies should follow in developing and maintaining their supplements are contained in the Federal Acquisition Regulation, subpart 1.3, as implemented by the Defense supplement. Specifically, these regulations require Military Departments and Defense agencies to control and limit issuance of supplemental acquisition regulations and establish formal procedures for the review of these supplements. Supplements should include only material unique to the Military

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[1] For purposes of determining what guidance was actually a supplement to the Federal Acquisition Regulation, issued pursuant to Section 1.301, we decided that if the guidance was numbered in accordance with the Federal Acquisition Regulation numbering system, the guidance was a supplement.

Department or Defense agency. Supplements should not contain material that unnecessarily repeats, paraphrases, or otherwise restates material contained in the Federal Acquisition Regulation or higher level agency acquisition regulations. In addition, except as required by law or authorized deviations, Service supplements should not conflict or be inconsistent with the Federal Acquisition Regulation or the Defense supplement. Finally, coverage not unique to a Military Department or Defense agency should be recommended for inclusion in the Federal Acquisition Regulation or the Defense supplement.

Discussion of Details

We reviewed 158 sections that comprised 2,840 lines randomly selected from the supplements issued by the Army, Navy, Air Force, and Defense Logistics Agency and found that overall, 44.8 per-cent 2/ of the lines did not comply with the established criteria.

FNA

[illegible]
NOT
CONSISTENT

In reviewing the Service supplements for compliance, we used the same methodology as in reviewing the Defense supplement. We reviewed each section and compared it to the Defense supplement and the Federal Acquisition Regulation. Further elaboration on the criteria and examples of each are contained in Enclosure 1. The results of our review are as follows.

Reasons for Noncompliance with Criteria	Line Count	Percentage
Duplicating/Paraphrasing Material	189	6.7
Clarification Required	615	21.7
Inconsistent Coverage	53	1.9
Not Unique to Military Department or Defense Agency	412	14.5
Total Noncompliance	1,269	44.8

We also categorized the noncompliance line count by coverage in the original supplements issued during 1984 and coverage added after 1984. From the 2,840 lines reviewed, 2,654 lines were in the original supplements. We took exception to 1,189 lines

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2/ Sample results are based on a confidence level of 90 percent and a precision factor of ± 6.2 percent.

(44.8 percent). This exception rate occurred because as with the Defense supplement, the Military Departments and Defense Logistics Agency had a relatively short time frame to develop their supplements. Of the remaining 186 lines added after 1984, we took exception to 80 lines (43.0 percent). We determined this exception rate occurred because the Military Departments and the Defense Logistics Agency had not established screening procedures to ensure that the changes made to their supplements complied with the Federal Acquisition Regulation. FF A

The above results could not be extrapolated to the individual Military Departments or the Defense Logistics Agency because the sample came from the four supplements. Although the most significant effect for noncompliance would be inconsistency with the Federal Acquisition Regulation, we estimated the exception rate for inconsistency to be only 2 percent. Furthermore, duplicating, paraphrasing, clarifying, and including coverage not unique to the Military Department and Defense Agency will lead to unnecessary verbiage in the Service supplements, resulting in the supplements becoming an increased administrative burden to users in the acquisition regulatory system. The results of the future audit will measure the Military Departments' and the Defense Logistics Agency's compliance on an individual basis.

Major Commands and Primary-Level Field Activities. Subordinate organizations to the Military Departments and the Defense Logistics Agency are also issuing supplements to the Federal Acquisition Regulation. Each of the Military Departments and the Defense Logistics Agency have implemented guidance in Section 1.304(c) of the Defense supplement requiring screening procedures to ensure that their subordinate organization supplements comply with Federal Acquisition Regulation 1.304. However, we did not perform a detailed review of these supplements to determine if such procedures were ensuring that the subordinate organization supplements comply with the regulation. We will perform a detailed audit of these supplements in the future.

Recommendations

We recommend that the Assistant Secretary of the Army (Research, Development and Acquisition), the Assistant Secretary of the Navy (Shipbuilding and Logistics), the Assistant Secretary of the Air Force (Research, Development, and Logistics), and the Director, Defense Logistics Agency:

A.1 ARMY
A.2 NAVY
A.3 AF
A.4 DLA

1. Require a line-by-line review of the supplements to the Federal Acquisition Regulation issued for their respective Military Department or agency and make necessary changes to comply with the Federal Acquisition Regulation, subpart 1.3.

2. Develop and implement review procedures for Service supplements to ensure continued compliance with the Federal Acquisition Regulation when changes are made to existing supplements or when additional supplements are issued.

A.5 Army
A.6 Navy
A.7 AF
A.8 DLA

MANAGEMENT COMMENTS AND AUDIT RESPONSE

A draft of this report was provided to the Assistant Secretary of the Army (Financial Management), Assistant Secretary of the Navy (Financial Management), Comptroller of the Air Force, and the Director, Defense Logistics Agency on March 23, 1987. We received comments from the Director, U.S. Army Contracting Support Agency, the Assistant Secretary of the Navy (Shipbuilding and Logistics), the Acting Deputy Assistant Secretary of the Air Force (Acquisition Management), and the Comptroller, Defense Logistics Agency. In addition, the Assistant Secretary of Defense (Production and Logistics) provided comments. All comments are in Enclosure 3.

The Director, U.S. Army Contracting Support Agency; the Assistant Secretary of the Navy (Shipbuilding and Logistics); the Acting Deputy Assistant Secretary of the Air Force (Acquisition Management); and the Comptroller, Defense Logistics Agency all concurred with Recommendation 1. The Army expects to have its line-by-line review completed by June 1988. The Navy stated that it completed a detailed review of one fourth of its supplement in October 1986. The methodology used for this review and the results were not brought to our attention during the survey. The Navy plans to continue reviewing one fourth of its supplement every 6 months. Therefore, it should be completed by July 1988. Air Force did not provide a time frame for completion. Therefore, we request that it provide completion dates when it comments on the final report. The Defense Logistics Agency plans to complete the review of its supplement by December 1987. All of the time frames provided are realistic.

Only the Defense Logistics Agency fully concurred with Recommendation 2. The Army, Navy, and Air Force indicated they had procedures in place to review changes to their supplements. However, during the audit we did not identify any formal procedures for the Army and the Air Force. The Army supplement did have procedures to review supplements issued by its major commands. However, there were no procedures in place for review of changes to the Army supplement. The Navy's guidance in Navy supplement 1.304 (90) refers only to activity level instructions, contract forms and contract clauses. There is no immediate reference to procedures for changes to the Navy supplement. The Air Force guidance is also directed to subordinate activities and not the Air Force supplement. If there are formal written procedures, the Army, Navy, and Air Force should provide them in their responses to the final report.

The Director, U.S. Army Contracting Support Agency provided extensive comments on the finding in the report. Since the Army has agreed to perform a line-by-line review of its supplement, despite its nonconcurrence with the finding, we have incorporated our detailed response to the comments in Enclosure 3.

Comments to the final report are required within 60 days. DoD Directive 7650.3 requires that audit recommendations be resolved within 6 months of the date of the final audit report.

A copy of this report is being provided to the senior officials responsible for internal controls within the Office of the Secretary of Defense, the Military Departments, and the Defense Logistics Agency because it identifies an internal control system weakness as defined by Public Law 97-255, Office of Management and Budget Circular No. A-123, and DoD Directive 5010.38. The lack of formal procedures for the review of changes to the Service supplements or the creation of additional supplements will negate the efforts made in the line-by-line review to ensure that the supplements are continually in compliance with the Federal Acquisition Regulation. Recommendation 2 is the proposed action to correct this internal control weakness.

Copies of the final report will be distributed to non-DoD activities listed in Enclosure 4. If you have any questions concerning this report, please contact Mr. James McHale on (202) 694-6273 or Ms. Kathleen Stanley on (202) 694-3603. The cooperation and courtesies to the audit staff are appreciated.

Richard W. Townley

Richard W. Townley
Deputy Assistant Inspector General
for Auditing

Enclosures

cc:
Secretary of the Army
Secretary of the Navy
Secretary of the Air Force

FEDERAL ACQUISITION REGULATION CRITERIA AND EXAMPLES OF NONCOMPLIANCE

Duplicate/Paraphrase

Duplication is a word-for-word copy of the Federal Acquisition Regulation or the Defense supplement. We did not take exception to verbiage that leads into implementing coverage. Paraphrasing is a restatement of the material contained in the Federal Acquisition Regulation or the Defense supplement giving the meaning of the material in another form.

Army

Army supplement clause 52.203-9000, "Covenant Against Contingent Fees," duplicates Federal Acquisition Regulation clause 52.203-5(a), "Covenant Against Contingent Fees."

Navy

Section 28.190(a) of the Navy supplement paraphrases Defense Supplement 28.106-70 concerning the review of bonds by the contracting officer.

Clarification

Clarification is coverage in the Service supplements that expands on higher level coverage, either by defining terms used in the Federal Acquisition Regulation or the Defense supplement, by providing examples, or by adding explanations.

Navy

Section 5.404 of the Navy supplement expands the guidance in Federal Acquisition Regulation 5.404 concerning the release of long-range procurement estimates by stating that long-range procurement releases may include planned requirements beyond the current fiscal year. Federal Acquisition Regulation 5.404 states that estimates may be published as far in advance as possible.

Air Force

Section 16.203-1 of the Air Force supplement categorizes the economic price adjustment clauses discussed in Defense Supplement 16.203-4(d)(3)(iv) as "abnormal escalation index" and "constant dollar index" clauses.

Inconsistent

Inconsistent coverage conflicts with the intent of the Federal Acquisition Regulation or the Defense Supplement.

Army

Section 17.290, "Addition of Options Clause or Quantities to Contracts After Award," of the Army supplement was inconsistent with Federal Acquisition Regulation 17.203, "Solicitation," which requires inclusion of the option clause in the original solicitation.

Air Force

Section 16.207-2 of the Air Force supplement provides for unlimited audits of firm-fixed-price level of effort contracts. The Defense Acquisition Regulatory Council had ruled against this provision in the Federal Acquisition Regulation.

Defense Logistics Agency

Section 49.9004 of the "Termination Manual" has not been updated to reflect the requirements of the Competition in Contracting Act of 1984.

Not Unique to the Military Department or Defense Agency

Not unique coverage includes policy guidance to a Military Department or Defense agency with no statutory or regulatory basis that supports the position that coverage is unique to the individual Military Department or Defense agency.

Air Force

Section 33.1059 of the Air Force supplement provides the address for the General Services Board of Contract Appeals.

Defense Logistics Agency

Section 15.470 of the Defense Logistics Acquisition Regulation pertains to the use of master solicitations. This topic is addressed in the Defense supplement, and it applies to all agencies.

ACTIVITIES VISITED OR CONTACTED

Office of the Secretary of Defense

Defense Acquisition Regulatory Council, Washington, DC

Department of the Army

Office of the Assistant Secretary of the Army (Research, Development, and Acquisition), Washington, DC
Army Contracting Support Agency, Washington DC
Army Materiel Command, Alexandria, VA

Department of the Navy

Assistant Secretary of the Navy (Shipbuilding and Logistics), Washington, DC
Naval Air Systems Command, Washington, DC
Naval Sea Systems Command, Washington, DC
Naval Supply Systems Command, Washington, DC
Naval Facilities Engineering Command, Washington, DC

Department of the Air Force

Assistant Secretary of the Air Force (Research, Development, and Logistics), Washington, DC
Air Force Systems Command, Andrews Air Force Base, MD
Air Force Logistics Command, Wright-Patterson Air Force Base, OH

Defense Agencies

Headquarters, Defense Logistics Agency, Alexandria, VA
  Defense Fuel Supply Center, Alexandria, VA
  Defense Personnel Support Center, Philadelphia, PA
  Defense Contract Administrative Services Region, Philadelphia, PA
Headquarters, Defense Mapping Agency, Washington, DC
Headquarters, Defense Communications Agency, Arlington, VA
Headquarters, Defense Nuclear Agency, Alexandria, VA

ENCLOSURE 2

SUBMITTED BY THE DEPARTMENT OF DEFENSE

IMPEDIMENTS TO BUYING COMMERCIAL PRODUCTS

The Defense Logistics Agency (DLA) buys to Department-developed specifications. For commercial products to be bought to a simplified commercial item description (CID), a decision must first be made by the specification preparing activity (a Military Department), along with the user community, that a commercial product satisfies its needs. The specification preparing activity must also prepare the CID, including quality assurance provisions to provide a standard for acceptance of noncommercially available items.

In doing this, DoD must, under current law:

--Comply with the Competition in Contracting Act provisions at 10 U.S.C. 2305, which require that specifications shall include restrictive provisions or conditions only to the extent necessary to satisfy the needs of the agency or as authorized by law. This effectively precludes us from limiting our sources to offers of commercial products exclusively, because offers of noncommercial products that can be determined to meet our minimum needs cannot legally be excluded. The 10 U.S.C. 2325 preference for nondevelopmental items did not eliminate the need to comply with 10 U.S.C. 2305. That is why the specification preparing activity must prepare the CID to make provision for both commercial and noncommercial items to be offered.

--Comply with the Small Business Administration implementation of 15 U.S.C. 631 et seq., which requires that if there are two small business manufacturers available, we must set our acquisition aside for the exclusive participation of small business. We might have several commercial sources, but if we have two small businesses available and if those two happen to be offering noncommercial items, we are precluded from using the commercial sources. The same opportunity to provide a noncommercial item must also be given to large businesses, when the conditions for a set-aside do not exist. Even if 10 U.S.C. 2305 was amended to permit the acquisition of commercial items exclusively, we would still be limited by the Small Business Act to buying from only small business commercial suppliers whenever there are two or more small business manufacturers available, to the exclusion of however many large business concerns may be able to offer the commercial item. Section 721 of P.L. 100-656 sought to provide some relief in this area by requiring that no more than 50 percent of clothing and textile (C&T) contract awards be restricted by business size. This has no effect, however, in t. small business preference awards were already less than 50 percent of C&T awards, while at the same time being much higher than the set-aside percentage for most other commodity groups bought by DoD.

--Comply with additional contract requirements that are unique to Government/DoD contracts and that hamper or preclude commercial item suppliers from offering their commercial items (e.g., DoD

Appropriations Act restrictions require any article of clothing to be domestically produced and that the raw material also be supplied from a domestic source; Buy American Act restrictions require that only domestic end products be acquired for public use, with certain exceptions; Cargo Preference Act restrictions require agencies acquiring supplies that may require ocean transportation to ensure that at least 50 percent (100 percent for DoD) of the gross tonnage of these supplies is transported on privately owned U.S.-flag vessels; cost or pricing data requirements, contract disputes, and termination as required by our contracts are not used or generally understood by manufacturing or distribution channels of such items.)

When buying commercial products, our method for buying should be commercial. It is incongruous to expect that suppliers of commercial items comply with all the trappings of a Government contract when supplying a commercial item, when those same trappings don't apply in the commercial world.

DLA/DoD has proposed legislation that would remove all of the statutory and regulatory impediments to buying commercial items exclusively. This bill was replaced with an Office of Federal Procurement Policy (OFPP) commercial acquisition bill that is currently in final review and is anticipated to be submitted to Congress by midyear 1989.

The OFPP bill would permit the purchase of off-the-shelf commercial items on the basis of commercial market acceptability. A number of exceptions are included, but the decision to use alternate authorized procedures rests with the contracting officer. The bill would also exempt commercial purchases from any requirement of law that prescribes contract terms and conditions or that prescribes preferences for any source or class of sources. Although we have some concern about the complexity of the proposed procedures, and the method used to exempt covered acquisitions from all other provisions of law leaves room for question, the OFPP bill would provide a procedure for purchasing commercial items that approximates commercial-style acquisition methods.

RESPONSES TO WRITTEN QUESTIONS SUBMITTED BY SENATOR HEINZ

ENCOURAGE THE USE OF STANDARDS THROUGHOUT THE MILITARY

Senator Heinz. Through its SHARP (Standard Hardware Acquisition and Reliability) Program, I understand that the Navy has successfully improved the reliability of many electronic components in its systems while reducing costs and easing inventory and repair problems. However, there remain obstacles to expanding the use of standards across the services. What actions are being taken to encourage the use of standards throughout the military?

Response. In 1984, at the Air Force Modular Avionics Standards Open Forum, the Navy Standard Electronic Modules (SEM) Program and the Air Force Integrated, Communications, Navigation, Identification Avionics (ICNIA) Program, personnel agreed to start working on a new module standard called "Format E". This new module size would be large enough to provide for the functionality required in advanced systems while minimizing the module cost. Since the Open Forum in 1984, SHARP personnel have continued to work with Air Force Personnel of the ICNIA Program and also the Pave Pillar Program Office. Several draft Format E specifications have been written and reviewed by Navy, Air Force, and contractor personnel. After a long period of review and negotiation, NAVSEA drawing 6133410 was released in April 1987 as an interim specification.

More recently, the Joint Integrated Avionics Working Group (JIAWG) has proposed that SEM E be used as the common building block for functionally interchangeable modules for the Air Force ATF, the Navy ATA, and the Army LHX programs. The SHARP program has hosted a workshop for the past two years on Standard/Common Module Challenges. The next workshop is scheduled for May 1990. Participation from all three services in the workshop has been good.

The technical working levels within the services and the logistics elements are very supportive of developing standards for use by all the services. Contacts are being initiated within the services with new weapon system program offices to discuss the benefits of SHARP utilization.

MAXIMIZING BENEFITS BY EXPANDING THE USE OF STANDARDS

Senator Heinz. Given that the development costs for standard electronic modules in programs such as the Poseidon and Trident, as well as in sonars, have already been borne by the Defense Department and the taxpayers, does it stand to reason the DoD should seek to reap the maximum benefit on that expenditure by expanding the use of standards to the greatest extent possible?

Response. We concur. The use of standards across multiple systems will provide cost savings to DoD because the design cost of a function does not have to be repeated for each new system or for multiple uses within a system.

To date, the SHARP program has identified more than 400 Standard Electronic Modules (SEM). New SEM are continually being added, thereby offering a broad and up-to-date selection of module functions. There are currently in excess of 250 different Navy systems which utilize SEM. In excess of 10 million modules have already been committed to service in these systems, which currently supports an industry base of over a dozen qualified vendors.

SEM have proven successful in meeting the objectives of improving reliability and reducing cost, and offer the potential of added benefits as expanded implementation of the diverse module families occur. The use of SEM has brought about cost savings of millions of dollars over and above the cost of incorporating the SEM discipline into the system design and development process. This is due to the fact that the average SEM is utilized in eight or more unique systems.

Such cost benefits can be attributed to the impact that the SEM Program has had on the system development phase by allowing use of existing module designs and by their competitive procurement from an active commercial market. Long-term system life-cycle-cost benefits of SEM can be even greater because use of SEM minimizes the impact of technological obsolescence and encourages meaningful economic innovation through functional specifications. Both intra and inter system commonality of SEM also contribute greatly to minimizing system life-cycle-costs.

SIMPLIFYING INVENTORY IN THE USE OF STANDARD ELECTRONIC MODULES

Senator Heinz. It is my understanding that the modular approach facilitated by using standard electronic modules (SEMs) reduces the mean-time-to-repair, as well as simplifying the inventory requirements in forward locations. If so, does this provide a sound reason for using standards, in general, whenever possible, and should standard electronic modules, in particular, be the design choice for DoD?

Response. We concur. The modular approach using SEM requires a lower skill level to repair a fault in a system. The mean time to repair is decreased due to the fact that it becomes a remove and replace procedure. The more often a standard module is used by all services and in multiple systems, fewer spares are required to support the systems.

If both SHARP hardware and the commercial hardware satisfy the full military application requirements and both are manufactured to an equal quality level, then the logistics differences should be minimal. However, most commercial hardware is not submitted to a qualification program similar to the SHARP qualification program. This qualification program has been shown to increase hardware reliability by a factor of four to one.

There are other logistics issues that must be addressed when commercial equipment is used in military systems. First, the Government will probably not own the documentation or data rights to the commercial equipment. This will complicate establishment of organic repair facilities. In fact, repair will probably need to be performed at the original equipment manufacturer's facility. Second, for commercial standards, the individual cards and components will almost certainly not be interchangeable from one manufacturer to another. This will require provisioning of spares for each manufacturer's equipment at the final equipment level if system readiness is to be maintained.

Today's SHARP standards are designed to be repairable and can be procured from multiple sources. Therefore, provisioning of repair components must be addressed. However, the government owns the performance specifications for the SHARP standards and has data rights as required to establish organic repair capabilities. Also, to the extent that standardization is achieved, the scope of the logistics problem is reduced because fewer unique configuration items must be supported. Benefits of the SHARP concept, such as competitive procurement, performance specifications, intersystem and intrasystem commonality, and higher reliability, all contribute to reducing the magnitude of the logistics support issue.

E. ADDITIONAL SUBMISSIONS FOR THE RECORD

IRVIN INDUSTRIES INC.

WORLD HEADQUARTERS

STEPHEN M GORDON
PRESIDENT

December 29, 1988

The Honorable Carl Levin
United States Senate
Washington, D.C. 20510

Dear Senator Levin:

Because reform of the Pentagon's procurement system will be a priority in this Congress, I thought you would find it useful to know about a recent Air Force procurement in which my company was involved.

Among other things, the Air Force appears to have ignored completely the provision in the 1987 Defense Authorization bill you authored requiring that preference be given to developmental items over non-developmental items. My firm manufactures a device now in service with the air forces of several NATO countries. But the U.S. Air Force, whose requirements are identical to those of the other NATO air forces, has commissioned another company to develop a device from scratch.

The way this procurement was handled by the Air Force also raises serious questions about conflict-of-interest and the choice between a cost-plus, sole source contract versus a fixed price contract arrived at through competitive bidding. I believe this is a situation, particularly in light of the current problems in procurement practices in the Pentagon and the Congressional directive in your amendment in which you may see a strong reason to make an inquiry to the Air Force.

Background of the Procurement

In February of 1987 the Air Force initiated a two-step formally advertising procurement for a production quantity buy of mechanical automatic parachute release mechanisms, devices which open a pilot's chute at a particular altitude once he has been thrown free of the aircraft by his ejection seat. With this type of procurement companies respond to step one with technical proposals, describing in detail what they would furnish the government were they awarded the contract. No price information

630 FIFTH AVENUE, NEW YORK, NEW YORK 10111
TEL (212) 977-2500

TELEX NOS 640879 Domestic
661248 International

is submitted. At this stage the purpose is to determine how many companies can produce an item meeting the agency's needs. Federal procurement regulations and the Competition in Contracting Act say that as many bidders as possible should be qualified. This ensures there will be vigorous price competition at stage two of the procurement when all bidders who qualified at step one submit their best price by sealed bid.

Irvin Industries, a New York-based company with plants in Michigan, California, North Carolina and Kentucky, as well as Canada and Europe, was one of at least three companies that responded to the Air Force's February 1987 solicitation. Irvin offered to supply a slightly modified version of the release now sold to the air forces of Canada, West Germany, Italy and Spain. Irvin had good reason to believe this release would meet with Air Force approval. For almost three years the Air Force had said (as its own documents demonstrate) that it wanted to buy the Irvin release and it had repeatedly assured Irvin that Irvin's release met the Air Force's minimum requirements.

The Elimination of Competition

Irvin was thus stunned when, in May 1987, the Air Force said that not only did the release not meet the Air Force's needs, but that it was the Air Force's judgment that the Irvin release could not even be modified to meet its needs. As a result of this determination Irvin was disqualified from step two of the competition. In fact, only one offeror was allowed to proceed to step two, thus eliminating entirely all price competition and effectively turning the "competition" into a sole source award to a company that had never before manufactured or sold a mechanical release.

What the Air Force said when it disqualified Irvin flatly contradicted every statement the Air Force had made to Irvin since the Spring of 1984 (and, as it turned out from subsequently obtained documents, also contradicted findings of its own technical experts). When Irvin confronted the Air Force about its prior representations, the Air Force denied it had ever made such statements. Irvin's suspicions were aroused even more when we learned that Scot Inc., the only company not excluded from step two, had retained as a "consultant" a former employee of the Air Force. This consultant had, until only months before, been deeply involved in the procurement of releases.

Irvin brought these issues before the General Accounting Office in a formal bid protest it filed in June of 1987. The GAO did not address Irvin's conflict of interest concerns regarding Scot's use of a "consultant" recently centrally involved in the Air Force decision-making on this procurement." And when Irvin stated that the Air Force's current views on the Irvin release were drastically at odds with what it had been telling Irvin for almost three years, the Air Force again simply denied making the earlier statements. It thus became Irvin's word against that of the Air Force; the GAO chose to take the Air Force's and dismissed the protest.

The Sole Source Contract

This was where matters stood until this past fall when two things happened. First, the Air Force announced the award of a contract to Scot. But whereas the February 1987 "Request for Technical Proposals" had asked for a fixed price and included a tight delivery schedule, the contract awarded Scot is cost-plus with delivery stretching out four to five years into the future. As for price, Irvin had offered to sell its releases to the Air Force in 1984 for about a third of what the Air Force estimates it will now pay Scot.

Another important difference between the contract Irvin bid on and the one Scot was awarded is that the original solicitation sought a non-developmental item. What the Air Force wanted, at least according to its "Request for Proposal," was an off-the-shelf product, a proven release that was ready to go. But, in apparent direct contradiction to the mandate of the Levin Amendment, which expressed Congressional preference for off-the-shelf contracts over developmental contracts, the Air Force changed its specification under the RFP and awarded a developmental contract. This means that Scot will be building a brand new, untested and unproven product, will be paid extra for the costs of a prototype and thus the government will bear all the risk.

The second thing that took place this past fall was that Irvin obtained copies of internal Air Force documents that confirmed that the Air Force had seriously misrepresented the facts to Irvin and to the GAO. These documents showed that the Air Force had indeed found that Irvin's release met its needs and was prepared to purchase 7500 units. We would be happy to make these documents available to you and your staff. This raises even more questions about the integrity of the process since, in response to a Freedom of Information Act request Irvin filed at the time of the GAO protest, the Air Force had said these documents did not exist.

Conclusion

Irvin recently filed a lawsuit in Federal District Court for the District of Columbia in an effort to force the Air Force to put this contract out for competitive bids on a fair and equal basis. I realize that you cannot and should not get involved in the merits of this litigation. Nonetheless, I believe Irvin's experience raises substantial questions of public policy that go to the integrity of the procurement process and Congressional policies in favor of competition and cost-efficient procurement actions.

I would very much appreciate the opportunity to meet with you in the near future to discuss these important issues and to secure your help in writing a letter of inquiry to the Secretary of the Air Force asking for the Air Force's reaction to the troubling facts involved here. I doubt that the Secretary is aware of the seriousness of what has happened and the extent to which fundamental procurement policies have been violated. I believe a letter of inquiry from you would help focus attention on the question of developmental versus non-developmental items and perhaps lead to a recognition that permitting Irvin to compete is in the best interest of the Air Force as well as the public.

I will call your office shortly after the first of the year to schedule an appointment with you and your staff.

Thank you in advance for your willingness to review this situation for us.

Sincerely,

Stephen M. Gordon

Stephen M. Gordon

Electronic Industries Association

Peter F. McCloskey
President

May 24, 1989

Hon. Carl M. Levin
Chairman
Subcommittee on Oversight of Government Management
Committee on Governmental Affairs
United States Senate
Washington, DC 20510

Dear Senator Levin:

On behalf of our witnesses before your Subcommittee hearing on May 16, dealing with implementation of commercial products preference legislation, I want to thank you for the opportunity of presenting the association's views. We appreciate your continued interest, and that of other members of the subcommittee, in trying to ensure appropriate and more complete implementation of this legislation by the procuring agencies. We look forward to continuing to work with you and your staff to that end.

I also want to take this opportunity to provide the enclosed materials as a supplementary submission for the record of the hearing. Attached are four examples of problems encountered by commercial products manufacturers in trying to supply the government with non-developmental items under commercial-style terms and conditions. We trust these will be relevant and useful in your ongoing efforts to address real-world problems in commercial products procurement.

Our final submission is the February 13, 1989 letter to the Department of Defense by the Council of Defense and Space Industry Associations (CODSIA), to which EIA was a signatory. This letter includes examples of specific problems in cost and pricing data submission requirements, and offers a proposed revision of the Federal Acquisition Regulation (FAR) to provide appropriate waivers for suppliers of commercial products and services.

We believe the CODSIA proposal continues to represent the best and simplest reform package to deal with the variety of cost and pricing data issues in commercial procurement. We are aware of other, parallel efforts underway in DoD to examine potential waivers or exemptions for commercial suppliers, and continue to urge acceptance of the CODSIA approach as the most reasonable and effective solution to the cost and pricing data problem.

Temporary Headquarters: 1722 Eye Street, N.W. · Suite 300 · Washington, D. C. 20006
2001 Eye Street, N. W. · Washington, D. C. 20006 · (202) 457-4900 · TWX: 710-822-0148

Again, your continued interest and involvement in oversight of the implementation of NDI preference legislation is much appreciated by our member company commercial product suppliers, and we were very pleased to have had a role in building the excellent hearing record established on May 16.

Sincerely,

enclosures

EIA Attachment One
Honorable Carl Levin
May 24, 1989

Example 1

In a 1987 Army/Air Force procurement for ADP equipment and peripherals, at least one EIA member company decided to "no bid" the procurement because of inappropriate terms and conditions and related impediments to commercial-style procurement. Unacceptable clauses included Source Inspection; Required Source for Jewel Bearings; and Specialty Metals Clauses. The RFP included other impediments to commercial suppliers, such as lack of standard acceptance requirements, maintenance, operating and software terms. There was a requirement that the same discount rate be applied on future purchases as the rate offered on the initial bid. A "most favored customer" provision required that future purchases could be made at terms and prices not higher than those offered to any other customers anywhere. Guaranteed requirements for machine "up time" and required replacement with new equipment for machine failures were substantially in excess of standard commercial practices.

EIA Attachment One
Hon. Carl Levin
May 24, 1989

Example 2

In 1984, there was a hail storm in the Munich area of Germany. Hail stones the size of baseballs damaged buildings, cars and airplanes. All commercial airplanes had repairs started immediately (next day) and completed for full operational service within three weeks (most within one week). The airlines were able to immediately authorize repairs and replacements for the commercial airplanes by a manufacturers "Airplane on the Ground" (AOG) team, with the airlines to be billed for completed work. The AOG team was on the job in 24 hours.

Also damaged (no worse than the commercial airplanes) were two U.S. military versions of some damaged commercial airplanes. Procurement of repair parts and preparation for repairs were not authorized for six weeks, although there was never any question as to the need for these repairs to the military airplanes. The delay in direction to proceed with repairs was due to constraints in the Government procurement system necessitating a final price be negotiated with the contractor before the work could be authorized.

If treated as the commercial airplanes were, the aircraft could have been repaired and flown away to their operating base in less than three weeks. Because they were not, the Government incurred increased maintenance, storage, and retest costs; and lost the availability of mission capable aircraft. Even after the authorization to start work, the procurement of repair parts was subjected to administrative processes that introduced additional delays. The military airplanes' repairs were not completed until five months after the damage, compared to two weeks for comparably-damaged commercial airlines. The differences were entirely attributable to the U.S. government procurement statutes, regulations and practices vs. commercial practices.

EIA Attachment One
Hon. Carl Levin
May 24, 1989

Example 3

A strong defense now and especially in the future requires American industry to be strong and remain competitive with global manufacturing, a particular concern in the semiconductor industry. Congress and the Executive Branch have also expressed a strong preference for the use of competition in government procurement and to increase the commerciality of purchases.

However, the FAR implementation and administrative interpretation of requirements for submission of certified cost and pricing data fail to recognize the broader concept of competition in this context, and are inconsistent with the economics of the U.S. semiconductor and related microelectronics industry, upon which DoD relies to provide advanced technology.

There is an inconsistency between FAR 31.205-26(e) and 15.804-3(b) in the definition of what constitutes adequate competition. FAR 31 requires that a competitive price is fair and reasonable only if it "results from an actual award" on that solicitation, in order to charge what would otherwise be allowable costs using FAR 15.804 "based on adequate competition" criteria. Also, FAR 15.804 allows Agency Head and Chief of Contracting Office waivers for the cost and pricing data requirement when the price is determined to be fair and reasonable, but DoD interprets that a waiver for 15.804 cost and pricing data does not waive FAR 31 allowability criteria. This contradiction effectively precludes use of intracompany transfers from separate business segments which predominately serve the highly competitive commercial semiconductor markets.

In material procurement, it is a common industry practice to obtain competitive bidding on package purchases, require single bids representing each supplier's best offer, and then source select the best overall value bid for further negotiation. Always requiring cost or pricing data to negotiate critically degrades the competition by limiting sources to only those who can provide cost or pricing data.

DoD's current practice of requiring cost or pricing data on Request for Proposals even on competitive procurements (firm fixed-price negotiated) forces primes and their subcontractors to supply and certify the data. To comply, U.S. semiconductor suppliers must segregate DoD processing and manufacturing from non-DoD. This isolation limits potential sources and also delays migration of advanced technology from commercial to DoD segments, even from sources that can provide cost or pricing data. Prime systems designers are forced to design only with suppliers and in technologies where cost and pricing data can be provided. Currently, as an example, the largest U.S. semiconductor supplier has not separated DoD manufacturing from commercial and subsequently refuses to accept business that will require submission of cost or pricing data. To establish a detailed Cost Accounting System to supply semiconductor product cost and pricing data to Public Law 87-653 standards would be harmful to the other 97% of their highly cost/technology competitive and strictly commercial operations.

EIA has written DoD on April 26, 1989 to urge support of the following recommendations or, at a minimum, approval of a class deviation in these areas for semiconductor products.

Specific Recommendations

Remove the inconsistencies between FAR 15.804 and FAR 31.205 by revising FAR 31.205-26(e)(2) from:

Is the result of "adequate price competition" in accordance with 15.804 and is the price at which an award was made to the affiliated organization after obtaining quotations on an equal basis from such organization and one or more outside sources that produce the item or its equivalent in significant quantity.

To:

Is based on "adequate price competition" or the certification of cost or pricing data is waived in accordance with 15.804-3.

EIA Attachment One
Hon. Carl Levin
May 24, 1989

Example 4

Medium Expendable Launch Vehicle (MELV) Request for Proposal

NASA has issued an RFP for MELV that significantly departs from any intent to procure ELV on a commercially reasonable basis. The RFP for MELV was issued on 7 March and includes terms that preclude the procurement from being a commercial transaction. Such terms include:

- The Government has the right to inspect and test all services called for by the contract.
- The Government shall have insight and approval into contractor performance. Geostationary Operational Environmental Satellite (GOES) also provided for this, but limited rights to "after delivery" of launch vehicle to the cape
- DCAA audit rights clause is incorporated
  - o Audit rights are not accorded under commercial programs
- The contractor must sign a certificate of wage determination
- The RFP does not contain a liquidated damages for Government delay clause, although the GOES contract contained such a provision, and the contractor may be penalized for liquidated damages for contractor delay (in addition to termination for default penalties).

COUNCIL OF DEFENSE AND SPACE INDUSTRY ASSOCIATIONS (CODSIA)

1722 Eye Street, N.W., Suite 300
WASHINGTON, D.C. 20006
•
(202) 457-8713

EIA Attachment Two
Hon. Carl Levin
May 24, 1989

February 13, 1989
CODSIA Case 22-87

Mr. Duncan Holaday
Director
Defense Acquisition Regulatory Council
ASD (A&L) DASD(P) DARS
c/o 3E791, The Pentagon
Washington, DC 20301-3062

Dear Mr. Holaday:

The undersigned member associations of the Council of Defense and Space Industry Associations (CODSIA) would like to bring to your attention an issue of major importance to our member companies providing commercial (non-mil spec) products to the Department of Defense and other government agencies. The requirement for commercial product suppliers to provide certified cost or pricing data to the government has long been a major constraint on companies' willingness and ability to do business with the government.

We are herewith requesting establishment of a DAR case effort to examine specific policy changes which we believe will have a markedly positive effect by waiving the requirement for submission of cost or pricing data in appropriate instances. By reducing some of these unnecessary requirements, we believe the government will benefit from an enhanced ability to acquire new technology, and will see increased competition in the procurement process as more companies find themselves able and willing to compete for government contracts.

Enclosed for your consideration is a memo and attached rationale concerning the specific changes we would like the council to focus on as it considers changes in this area. While numerous other barriers must be overcome, we believe adoption of this proposal would be a positive first step toward accomplishing our mutual objective of increased commercial product procurement.

We appreciate your consideration of this proposal, and our representatives are available to meet with you to discuss it further should you or members of the council wish to do so.

Sincerely,

Don Fuqua
President
Aerospace Industies Assn.

Jean A. Caffiaux
Senior Vice President
Electronic Industries Assn.

John L Pickitt

John L. Pickitt
President
Computer & Business Equipment
Manufacturers Assn.

J R Iverson

J. Richard Iverson
President
American Electronics Assn.

Wallace H. Robinson, Jr.
President
National Security Industrial Assn.

SUPPORTING EXAMPLES

NEWLY INTRODUCED COMMERCIAL PRODUCTS: In August 1986, an IFB (2-step bid sample) came out for a cable tester. After the technical evaluation (1st step), only one bidder was acceptable. The acceptable vendor offered a "B" model for evaluation which was the updated and replacement model for an older "A" model. In April 1987 an RFP was requested of the acceptable bidder (a commercial vendor) requiring a SF 1412. The commercial vendor, in May 1987, submitted a SF 1412 on the "A" model since the "B" model was too new to have a sales history. In June 1987 DoD requested cost and pricing data on the "B" model. In July 1987 the commercial vendor responded that the "B" model product was similar and a planned replacement for the "A" model. After three SF 1412 submissions and rejections, in April 1988 a SF 1412 was submitted, now based on actual commercial sales of the "B" model because the product had been on the market for 6 months, and was accepted.

DISCONTINUED COMMERCIAL PRODUCTS: Commercial vendor manufactured thermal printer driven by large computer. Technological capabilities changed and thermal printer became obsolete. Commercial customers moved to new technology while government continued to buy thermal printers for replacement purposes and to meet overall systems design specifications based on long lead times. Once commercial sales dropped below 35 percent, product no longer qualified for exemption from submission of certified cost or pricing data. Commercial vendor, unable to supply cost or pricing data, had to either seek a waiver or limit sales to contracts under $100,000.

SPARE AND REPLACEMENT PARTS:

EXAMPLE 1: Assemblies containing repairable components of commercial test equipment are not normally repaired by commercial users by replacing individual components. The commercial users usually buy maintenance and service contracts that result in sales of modular replacement units being buried in repair orders and consequently, not easily traceable. DoD relies on the use of modular replacement units where the entire circuit board is replaced in the field but then the defective board is sent to a depot for repair. Because the entire circuit board, although priced in a catalog, is rarely sold to commercial users, the circuit board does not meet regulatory definition of "substantial quantities".

EXAMPLE 2: Certain spare or replacement parts for commercial products have a design life that far exceeds the design life for the whole commercial product. As a result, commercial customers rarely purchase those parts. DoD, however, with unique stockpiling requirements will purchase significant quantities of those long design life spare parts. Because few commercial customers buy those spare parts, they do not meet the regulatory definition of "substantial quantities". As a result, cost or pricing data can be required.

SKEWING OF SUBSTANTIAL QUANTITIES TEST: Sales of commercial oscilloscope had traditionally been split 80 percent to the general public and 20 percent to the Government. A single buy by the Air Force of 8,000 units reversed the split in sales so that the product was no longer considered exempt from submission of cost or pricing data.

REVISED FAR 15.804-3(c) LANGUAGE

(c) Established catalog or market prices. A proposal is exempt from the requirement for submission of certified cost or pricing data if the prices are, or are based on, or for discontinued items were based on at the time of notice of discontinuance, established catalog or established market prices of commercial items sold in substantial quantities to the general public.

i. A proposal for a newly introduced commercial product is exempt from the requirements for submission of certified cost or pricing data if the prices are based on established catalog or established market prices for the newly introduced commercial product offered for sale to the general public.

ii. A proposal for spare or replacement parts for commercial items where the commercial items are offered for sale to the general public is exempt from the requirement for submission of certified cost or pricing data if an offeror submits a certificate of commercial pricing certifying to the best of the knowledge and belief of the offeror, the price proposed in the offer does not exceed the lowest commercial price at which the offeror sold such parts during the most recent regular period for which sales data are reasonably available. In order to qualify for this exemption, the terms of the proposed purchase, such as quantity and delivery requirements, should be sufficiently similar to those of the commercial sales that the catalog or market price will be fair and reasonable.

(1) "Established catalog prices" must be recorded in a form regularly maintained by the manufacturer or vendor. This form may be a catalog, price list, schedule, or other verifiable and established record. The record must (i) be published or otherwise available for customer inspection and (ii) state current or last sales price to a significant number of buyers constituting the general public (see subparagraph (4) below).

(2) "Established market prices" are current prices that (i) are established in the course of ordinary and usual trade between buyers and sellers free to bargain and (ii) can be substantiated by data from sources independent of the manufacturer or vendor.

(3) An item is "sold in substantial quantities" only when the quantities regularly sold are sufficient to constitute a real commercial market. Nominal quantities, such as models, samples, prototypes, or experimental units, do not meet this requirement. For services to be sold in substantial quantities, they must be customarily provided by the offeror, using personnel regularly employed and equipment (if any is necessary) regularly maintained solely or principally to provide the services.

(4) The "general public" is a significant number of buyers other than the Government or affiliates of the offeror; the item involved must not be identified for Government end use. Any sale

other than a direct sale to an instrumentality of the U.S. government for government use is a commercial sale.

(5) A price is "based on" a catalog or market price only if the item being purchased is sufficiently similar to the catalog- or market-priced commercial item to ensure that any difference in prices can be identified and justified without resort to cost or price analysis. For discontinued items, "based on" shall mean the last published or market price at which sales of the item were made to the general public, increased by an agreed-to annual price escalation factor that allows for increased manufacturing and inventory carrying charges.

(6) If an item is similar to a commercial item for which there is an established catalog or market price at which significant quantities are sold to the general public, but the price proposed is not based on this catalog or market price (see paragraph (5) above), the contracting officer may, if doing so will result in a fair and reasonable price, limit any requirement for cost or pricing data to those data that pertain to the differences between the items. When there is a difference between the catalog or market price and the proposed price to the government, the offeror shall bear the burden of establishing reasonableness of the incremental cost.

(7) "Commercial items" are supplies or services regularly used for other than Government purposes and sold or traded to the general public in the course of normal business operations. Or, in the case of a newly-introduced product, an item should be considered a commercial item if the commercial vendor offering that item is: in the commercial business of producing such type items on a regular basis, the new product is within the family of products sold commercially, the offeror has publicly announced the item as a new product line and is in production of such items.

(8) Even though there is an established catalog or market price of commercial items sold in significant quantities to the general public, the contracting officer may require cost or pricing data if (i) the contracting officer makes a written finding that the price is not reasonable, including the facts upon which the finding is based, and (ii) the finding is approved at a level above the contracting officer.

(9) (added) "Discontinued items' are items that are no longer supplied by the manufacturer or vendor to the commercial marketplace but are required by the Government. For such items, exemption from submission of cost or pricing data shall be determined by applying the criteria in (c) above to sales for the appropriate period immediately prior to the supplier's notice to the Government of intent to discontinue the item. The first favorable determination of commerciality shall be considered a class determination and shall apply to all additional purchases

of the item, including any equivalent remanufactured items that may be substituted.

REVISED FAR 15.804.3(f) LANGUAGE

(f) Verification. (1) When a prospective contractor requests exemption from submission of certified cost or pricing data, the contracting officer shall ensure that applicable criteria in either paragraph (c) or (d) above, as appropriate, are satisfied before issuing the exemption.

(2) SF 1412 lists three categories of sales related to the established catalog price of a commercial item sold in significant quantities to the general public: A) Sales by other than competitive procedures to the U.S. Government or to contractors for U.S. Government use; B) Sales at catalog price to the general public; and C) Sales to the general public at other than catalog price. Although "significant quantities" cannot be precisely defined (see subparagraph (c)(3) above), the following guidelines are provided for determining whether exemption claims submitted under the catalog price provision of SF 1412 meet the "substantial quantities" criterion:

(4) (added) For vendors with GSA Multiple Award Schedule contracts, SF 1412s are not required for products where GSA has determined that such products are "commercial items", and such products are included in a Schedule contract which currently is in effect.

MEMORANDUM FOR DIRECTOR, DAR COUNCIL

SUBJECT: Revision of FAR 15.804-3, Exemptions from Submission of Cost or Pricing Data

I. PROBLEM:

1. FAR 15.804-3(a) provides exemptions to the requirement for submission of cost or pricing data when it is determined that prices are based on adequate price competition, are based on established catalog/market prices of commercial items sold in substantial quantities to the general public, or are set by law or regulation. Newly introduced commercial products and discontinued commercial products will likely not meet the substantial quantities test for exemption from submission of certified cost or pricing data. Further, certain modular replacement assemblies of commercial products (e.g. circuit boards) required for stockpiling purposes by DoD, but generally not purchased by commercial customers, also may not meet the substantial quantities test. Additionally, commercial customers often buy maintenance and service contracts, resulting in sales of replacement parts being buried in repair orders and not easily traceable. Lastly, a substantive, competitive Government purchase of a commercial product can skew the substantial quantities test so that certified cost or pricing data may be required.

2. Most commercial vendors will not provide cost or pricing data on commercial products to the Government, or to any other customer, for several reasons:

A. incompatibility of commercial accounting systems with specific government requirements;

B. unreimbursed costs of collecting and providing such data;

C. administrative burden that requires additional paperwork and personnel training;

D. basic company policy that prohibits disclosure of cost data and pricing methodology.

3. Section 2306a of Title 10 U.S.C. requires offerors, contractors, and subcontractors to make cost or pricing data available on negotiated contracts over $100,000. Section 2306a(b) exempts offerors, contractors, and subcontractors from submitting cost or pricing data on negotiated contracts when the price agreed upon is based on adequate price competition or established catalog or market prices of commercial items sold in substantial quantities to the general public. The term substantial quantities" is not defined by statute but rather is defined in FAR 15.804-3(c)(4). Commercial vendors, faced with a solicitation requirement to provide cost or pricing data, must either provide the data or seek an exemption. Commercial vendors must enter into time consuming and costly negotiations with Government contracting officers or be precluded from competing and from remaining competitive.

II. RECOMMENDATIONS:

1. Amend FAR 15.804-3(c) to exempt newly introduced commercial products, discontinued commercial products that are being sold at established catalog prices, and low volume spare or replacement parts that are sold at established catalog prices from the requirement for submission of cost or pricing data.

2. Amend FAR 15.804-3(f)(2) to include in Category A only those sales by other than competitive procedures in the category of "Sales to the U.S. Government or to contractors for U.S. Government use" for purposes of determining an exemption from submission of cost or pricing data.

3. Amend instructions to offerors submitting claim for exemption from submission of cost or pricing data on Standard Form 1412 (Instruction 9) to read as follows (addition underlined):

> "Item 9. (a) Include in Category A all sales by other than competitive procedures of the catalog item (a) directly to the U.S. Government and its instrumentalities and (b) for U.S. Government use (sales directly to U.S. Government prime contractors, or their subcontractors or suppliers at any tier, for use as an end item, or as part of an end item, by the U.S. Government.

III. DISCUSSION:

1. Commercial vendors that do not submit cost or pricing data are prohibited from selling newly introduced commercial products, discontinued commercial products, and spare and replacement parts to the government that do not meet the substantial quantities test. Commercial products in these three categories likely will not meet the regulatory "substantial quantities" test for exemption from submission of certified cost or pricing data. FAR 15.804-3(c) defines "sold in substantial quantities" to mean "only when the quantities regularly sold are sufficient to constitute real commercial market". FAR 15.804-3(f) further defines substantial sales to mean that at least 55 percent of the commercial product sales are to the general public at catalog or other prices and sales at catalog prices comprise at least 75 percent of all general public sales. The substantial quantities test is not met (FAR 15.804-3(f)(B)(2)(ii)) for commercial products where less than 35 percent of total sales are to the general public.

2. A substantive competitive government purchase of a commercial product can skew the "substantial quantities test" so that certified cost or pricing data may be required. Under current regulations, commercial vendors are penalized for competitive commercial product sales to the Government. Commercial vendors that do not submit cost or pricing data for commercial products and that sell a large number of commercial products to the Government, either though competitive or noncompetitive sales, may be precluded from selling products to the Government until sales to the general public surpass Government sales.

Attachments
1. Supporting Examples
2. Revised FAR 15.804-3(c) Language
3. Revised FAR 15.804-3(f) Language
4. Standard Form 1412

ALUMINUM COMPANY OF AMERICA
ALCOA BUILDING · PITTSBURGH, PENNSYLVANIA 15219

1989 May 25

The Honorable Carl M. Levin
Chairman
Subcommittee on Oversight of Government
Management
442 Hart Office Building
Washington, DC 20510

Dear Mr. Chairman:

I am writing to express Alcoa's views on DOD's procurement of commercial, non-development items which has been the subject of a recent hearing in your subcommittee.

Alcoa is a commercial company which develops, manufactures, and sells aluminum, titanium and other non-ferrous products to the commercial marketplace. As this market includes commercial aerospace customers, it is inevitable that some product finds it way to defense programs, frequently in derivatives of commercial aircraft but sometimes in unique military aircraft. The volume of our business that is defense-related, and practically all is at the subcontract level, varies from 5% to 7% annually.

Alcoa has the largest nonferrous metals laboratory in the free world dedicated to developing unique and superior products for these markets. Very little funding comes through DOD sources for our work to invent new products or processes. We do this work mostly on our own funds. [illegible] have developed advanced aluminum alloys for commercial transports. These alloys are also very attractive for military aircraft and have been specified by defense prime contractors for use on the F-14, F-15, F-16, F-18 and C-17 and other new aircraft in development.

In most cases, these alloys are patented, and are commercial, non-development items which we make available to both the commercial and defense markets here and abroad. It has been our experience that defense contractors shun sole source items due to procurement regulations even though they might be uniquely superior products. In the instance where a sole source aluminum alloy has been specified because it enables performance goals to be achieved, the government's contracting officer, or the purchasing agent for the prime contractor, asks for cost pricing data, SF1411 forms. In their eagerness to obtain certified cost or pricing data to protect themselves, they overlook the "based on" exemption provision of FAR 15.804-3(b) (3) which clearly provides for exemption resulting not only from direct competition but also from the use of price analysis to assure a fair and reasonable price. This over-zealous approach in requesting cost or pricing data, rather than exercising the exemption, causes an administrative burden for commercially oriented companies and creates added hazards because of the possibility of incorrectly certifying data due to commercial rather than a defense orientation within the company.

The "catalog or market price exemption" SF1412 is often of little practical use due to the restrictions on percentages of commercial versus defense sales. Waivers by the head of the agency, although provided by the FAR, are rarely given and do not provide a practical alternative as prime contractors avoid requesting such waivers.

I can assure you that the failure of these officials to properly exercise the exemption provision does cost the government - in terms of lost participation by commercial concerns and by failure to obtain the most cost efficient end product.

To summarize, we can sell these uniquely superior aluminum products to commercial markets, domestic and foreign, and to foreign military markets but find it difficult to sell to our own Defense Department due to the restrictions imposed by Cost or Pricing Data Requests.

We strongly urge that legislative remedies be sought since the regulatory exception provisions are not used.

Sincerely,

Vincent R. Scorsone
Vice President
Aerospace & Industrial Products

VRS:s/E45

digital

David J. Burke
Manager
Federal Policy Office

Digital Equipment Corporation
1331 Pennsylvania Avenue, NW, Suite 645
Washington, DC 20004
202.383.5615, DTN 427.5615

May 26, 1989

The Honorable Carl Levin
Chairman, Subcommittee on Oversight
of Government Management
Committee on Government Affairs
United States Senate

Dear Senator Levin,

Digital Equipment Corporation ("Digital") appreciates the opportunity to submit written testimony in support of the subcommittee on Oversight of Government Management review of section 907 (C) of the Defense Acquisition Improvement Act of 1986 (Public Law 99-661), regarding the Department of Defense ("DoD") efforts to increase the procurement of non-developmental items (NDI) and to remove impediments to commercial product acquisition.

In our testimony we identify three policy level issues which we believe block cost-effective acquisition and use of U.S. commercial computer systems and services by DoD and other Federal agencies:

- o Absence of guidelines in the GSA Delegation of Procurement Authority (DPA) process that maximize acquisition of commercial solutions and encourage use of commercial practices,
- o Improper use of large requirements contracts to purchase commercial systems and services, and
- o Continued use of inappropriate or proprietary specifications; or "de facto standards" which, in reality, are proprietary product specifications that have achieved significant market penetration.

Our testimony continues with an outline of Digital's three-year unsuccessful attempt to offer GSA a workable commercial contract for use by all Federal agencies. We conclude by urging Congress to pass legislation that states a preference for commercial solutions, requires agencies to express requirements in functional terms and mandates use of industry standards approved through the voluntary industry standards process and the

Digital Equipment Corporation
1331 Pennsylvania Avenue, N.W., Suite 600, Washington, D.C. 20004-1703
202.383.5600

Department of Commerce, National Institute of Science and Technology's Federal Information Processing Standards (FIPS) program.

Delegation of Procurement Authority

The Brooks Act gave GSA authority and responsibility for government-wide acquisition and management of computer systems. Over time, as agencies became more "computer proficient," much of the actual procurement work was delegated to the individual agencies. To ensure that the overall management of an agency was sound, the Paperwork Reduction Act of 1980 required a triennial review of an agency's computer acquisition plans; in effect, additional assurance that individual agency procurement requests were sound and were being executed in accordance with an overall plan.

In actual fact, the DPA process has seldom worked well. Protest proceedings and GAO audits of agency information resource management (IRM) point toward badly planned and badly executed acquisitions, the most recent being the multiple vendor complaint that a major Navy buying agency was specifying to a level of detail that significantly restricted competition. In another case involving an Army National Guard purchase of computers using an existing U.S. Army requirements contract called CONUS MINI, $18 million in purchased systems stood idle because an additional $40 million of required software conversion was not provided for in the planning phase.

In response to such criticism, GSA has reduced dollar thresholds for certain agency "blanket" DPAs, required agencies to submit additional paperwork and increased the resources for review teams examining agency IRM procurement and management performance.

While each of these corrective actions might have some merit, we believe not enough effort is being devoted to policy level guidelines that outline what is expected of agencies in their planning and execution. For example, agencies could be instructed that planning review, whether triennial or in response to a specific agency request for a DPA, will require that all feasible commercial solutions be considered and that no custom-built or proprietary solution would be approved until all commercial solutions were exhausted. Similarly, agencies would be required to demonstrate that the agency, not the contractor, was retaining control of the integration portions of a program.

Use of Requirements Contracts

With respect to the acquisition of computer systems, in the past few years it has become popular to write requirements-type contracts to accommodate many user needs at many locations. These types of contracts have been used for other types of procurement as long as the Federal Acquisition Regulation (FAR) system and its preceding regulations have existed. However, Digital strongly believes that, with respect to the acquisition of computer systems and services, requirements contracts are often misused and that their pitfalls outweigh their benefits.

The chief and sometimes only benefit of a requirements-type contract is lowest price. Requests for proposal that forecast thousands of systems to be purchased usually attract many vendors and achieve lowest prices not otherwise achievable; but large scale requirements contracts carry hidden costs that have incalculable effects on both vendors and users. Among those long-term effects are planned obsolescence and inhibited technology growth usually caused by the presence of so-called "standards" that are in reality proprietary specifications. If the contract requires mature technology -- to the point of reducing the procurement to a commodity buy -- vendors will be discouraged from investing in Government focused innovations and may even be discouraged from pursuing further Government business entirely.

From among many examples, we chose two: The 1985 National Security Agency's "Agency Standard Host (ASH)" contract and the more recent GSA Federal Telecommunications System (FTS-2000). ASH was specified to serve most all of NSA's general purpose analysts' support for several years. To accommodate NSA's many and varied needs, the procurement was, in retrospect, overspecified. The low bidder made product performance changes in order to be responsive to the specifications. Lacking the quality assurance found in a more typical commercial off-the-shelf product, the product offered on contract was not well received by users and thus the selected offeror never achieved anywhere near the forecast order rate.

The outcome of FTS-2000 is yet to be determined. However, before the first system was delivered, several agencies asked to be excluded from mandatory participation. The issue was forcing agencies to use one of only two vendors for networking services, irrespective of user requirements. One trade newspaper editorial called FTS-2000 "a requirements contract on steroids."

These examples also highlight a need to more carefully scrutinize and evaluate life cycle costs (LCC) and to make LCC a major factor in source selection. We are aware of Government contracting persons who are quick to argue that weighting LCC factors moves the source selection process away from primarily quantifiable evaluation techniques into heavy reliance on judgmental factors. We submit that there are good life cycle techniques in use by large commercial customers that can by adapted to Government procurements. In cases where the Government has evaluated bids based on documented life cycle costs, frivolous protesting has been rare.

The current industry and user consensus on large requirements contracts is that agencies should divide computer projects into pieces, avoid too much detail in their long-range plans and more carefully scrutinize bidder qualifications, other than just price, to include past performance. In late 1988, the Office of Management and Budget (OMB) Information Technology Advisory Committee (ITAC) called for "breaking long-term systems into easily managed parts." In other words, most information systems don't lend themselves to requirements buys because of their complexity and the wide variety of solutions and contingencies these acquisitions attempt to address. Requirements contracts tend to limit the technology offered by an industry in which rapid advances are the rule.

Digital's conclusions are similar: Requirements contracts succeed best when used in support of expansion or augmentation of an installed base where tight specifications are appropriate or where they are capable of supporting multiple solutions that are not force-fitted. Requirements contracts are not appropriate for large acquisitions involving a variety of applications, system components and integration. Requirements contracts fail when they are (1) not based on functional specifications, (2) do not offer a full set of tools and (3) do not respond to real customer needs, as opposed to a source-selection committee's general assumption of needs.

Use of Proprietary Specifications or "De Facto" Standards

Federal procurement standards policies are being interpreted to allow procurement officials to specify, in contract requirements, proprietary products which have achieved significant market penetration as if they had been adopted as formal consensus standards by industry and the Government. In general, this results in exclusion from bidding of vendors who do not offer the specified proprietary product. At the very least, the competitive playing field becomes less than level when proprietary products are mandated.

Thus, as was the case with large requirements contracts, the Government is moving in the standards area in a direction that stifles a creative technological environment. Since most of these types of specifications are based on mature technologies, the Government is rewarding certain manufacturers for achieving reductions in manufacturing costs rather than rewarding vendors and manufacturers who achieve cost reductions through technology innovation. In other words, the procurement process is penalizing companies who are improving computer systems technology and rewarding companies, most notably off-shore competitors, who compete on lower manufacturing costs, using selected components when there is a chance of displacing system vendors.

Voluntary standards are the heart of the commercial solution. industry built its standards environment on voluntary commitments because companies agreed that standardization should be at the "user interface" level, where solutions match functional requirements, where individual vendors would be allowed to be creative and add value and to convert state-of-the-art concepts into practical applications. Conversely, the by-fiat designation of a proprietary product specification as a "standard" will, over time, serve to "lock in" the user to a single product, thus restricting competition for future buys and increasing future conversion costs. In addition, such a designation without sole-source justification constitutes a violation of both competitive procurement rules and the regulatory requirements of the Federal standards process.

Digital applauds the National Institute of Science and Technology (NIST) for its increasingly active role in in the voluntary industry standards process and urges this Subcommittee to support NIST in its endeavors to be the Government voice in standards matters. The use of inappropriate or proprietary specifications, or "de facto" standards in lieu of recognized voluntary industry standards or functional specifications should only be tolerated under sole-source procurement rules.

To summarize, there are three key standards messages we wish to leave with this Committee:

- Standardize on interfaces to allow innovation of components without impacting overall system functionality. MAXIMIZE THE GAIN in areas such as performance and capability. MINIMIZE THE STRAIN of incorporating new technology.

- It is wrong to standardize on a proprietary product because that leads to technology stagnation and ultimately to a commodity mentality in which price is the only determinator. Offerors who compete in such an environment usually offer only the minimum functionality to win, not the most long-term cost-effective solution. It also invites devastating off-shore competition.

- Standardizing on a proprietary product reduces overall R&D investment incentive. Only the holder of the proprietary rights may choose to invest, others simply comply and the holder may limit his R&D investment if the current product is adequate for market conditions.

Towards a More Commercial-like Multiple Award Schedule System

Digital believes that a major opportunity exists for the DoD and other federal agencies to acquire commercial off-the-shelf computer systems and services at significant additional savings over current prices using an existing government-wide contract system. The system is the GSA Multiple Award Schedule (MAS) System which annually supplies over $2 billion in commercial computer products and services to DoD and other federal agencies. The opportunity is the realization of lower price offerings when certain non-commercial contract clauses are removed. Digital recommends that immediate steps be taken to evaluate this opportunity using a contract test program to measure savings achieved under a commercial contract as compared to the present contract procedures used in the MAS program.

The idea of a commercial-like contract that would more closely approximate the business relationship between buyer and seller in the commercial market place, yet still afford the Government buyer the contract protection required by public law, was first presented by Digital as a real proposal in April 1987. The idea was rooted in two Packard Commission recommendations; the first recommended that "Rather than relying on excessively rigid military specifications, DoD should make greater use of components, systems and services available "off-the-shelf". The second recommendation urged "...substantially increased use of commercial style competition, emphasizing quality and established performance as well as price."

Digital, and other commercial computer system vendors, shared a vision that a modified MAS system would function well in a commercial business setting and could be used to more forcefully exploit savings available in the commercial marketplace. Latest figures project that the Federal Government will spend about $18.5 billion on computers and related telecommunications in FY90. (Most of this spending is for commercial or modified commercial systems and the the DoD accounts for about half this spending) Over $2 billion of the total spent by all agencies is accountable using the GSA MAS system as a procurement vehicle. If as little as a 5% reduction in prices could be achieved by adopting commercial practices, the Government would realize an annual savings of $100 million. If the new commercial-like contract form proposed below works for the MAS system and could be applied to other contract strategies, additional savings would dwarf the $100 million mark.

What stood in the way of any real changes to the MAS system was a GSA policy (1986 version) entitled, "Policy Statement on Multiple Award Schedule Contract pricing Arrangements." Much of what is contained in that document is easily reconcilable to commercial practices. However, to put Digital's commercial contract alternative in perspective, we need to first outline a few key problems with the MAS policy.

The GSA's policy statement establishes the concept of the "most favored customer" (MFC), i.e., that customer receiving "an offeror's best discount. GSA then imposes a burden on offerors to justify, in quantitative terms, the difference between the MFC discount and that offered to the Government.

The GSA and the offeror ultimately agree on a price/discount and a customer or category of customers. A "Price Reduction" clause (GSAR 552.238-70) is included in the contract. This clause provides that any pricing changes (defined as changes in prices, discounts, or other terms and conditions) that disturb this relationship to the Government's detriment during the contract's term must be reported to the Government; a price reduction to the Government "to the extent necessary to restore .. the original relationship" then results. The offeror also must provide the GSA all data necessary to establish its negotiation objective, determine price reasonableness, and justify the Government/MFC price differential. Data on "price reductions" is provided throughout the term of the contract.

The point of the Multiple Award Schedule is to allow GSA to contract for standard commercial products for the use of Government agencies. The benefits of commercial contracting to the Government, and the need for greater Government efforts in this regard, have been recognized on numerous occasions. The current MAS policy, however, prescribes contracting for commercial products and services without standard commercial terms, and without using standard commercial negotiation techniques. Under these circumstances, many of the benefits of commercial contracting are lost. GSA could achieve many of these benefits by unburdening itself of the MAS policies discussed above, and adopting a more "commercial" approach to contracting for these products.

Digital's Alternate MAS Proposal

While the observations about current Government acquisition policy are important, without operational changes they remain words and ideas. Digital has been attempting for the last three years to actualize the finding of the Packard Commission by proposing a commercial process to acquire commercial products on the GSA Series 70A Schedule.

Three proposals have been made to GSA. Each year on the due date for the submission of the annual GSA solicitation response, Digital has included an "alternate" offer containing significantly lower prices as consideration for the removal of certain non-commercial contract clauses. In April 1987, the proposal used was based on Digital's commercial business agreement for volume purchasers. It however, did not take into account the statutory requirements with which the agency would have to either comply or seek a change. GSA rejected this proposal. The second year (April '88) proposal incorporated the statutory and regulatory requirements; however, there were differences from GSA policy and regulation which required evaluation. GSA and Digital agreed to table this proposal as it would not be possible to complete negotiations of the annual Schedule in a timely manner. In this year's proposal, submitted in April 1989, we have narrowed the differences to two terms which have no basis in law and which only impact GSA policy. GSA's initial response is that the complexity and breadth of the proposal require that the conventional response be considered before the alternate. We have agreed to do this with GSA but vigorously expressed our hope that there will be time at the conclusion of negotiations to pursue the alternate.

What we have seen over the last three years with GSA procurement personnel is that they are not well positioned to elevate issues which would effect change, yet the contract proposal is one of a limited number of forums in which commercial industries can propose change. Therefore some management initiative for decisive action is required on the part of Government to make this work!

We recommend first that GSA establish a program manager role for the GSA Schedule at a level which can manage change to policy and procurement process. GSA already has an excellent pilot program named "Trail Boss" to train program managers. We suggest that the appointment and enfranchisement of a trained GSA MAS program manager would effect changes beneficial to the Government and Industry and encourage greater industry participation in selling their products and services to the Government.

Our second recommendation is that GSA, on an experimental and demonstration basis enter into a commercial-like contract such as the one Digital has proposed. The differences between Digital's proposed commercial approach and the current MAS contract framework are first, reducing the data collected to that which is used for negotiation (emulating a commercial practice) and second, restricting the audit review process to the establishment of forward discounts.

The resulting commercial-like agreement would allow the Government to not only continue to attain volume discounts at the beginning of the agreement, but also would allow individual orders against the contract to attain even higher discounts by leveraging prevailing market conditions at the time of order or the degree of competition effecting the order. By comparison, the current practice is to include a Price Reduction clause in the contract which requires that once an individual order concession is made above the initial discount, all orders for those products would be at that discount regardless of the circumstances of the subsequent order. Hence, under the current MAS contract, no additional price reductions created by future market conditions can be realized. A buying agency is then faced with the alternative of accepting the GSA price or making an open market solicitation for proposals. The open market process takes from 12 to 15 months for orders over $25,000 as compared with approximately 1 to 3 months when ordering under the GSA Schedule. The additional cost to both the Government and Industry is in proportion to the additional time required.

Digital has proposed an additional discount for modification of these two terms which would result in estimated savings to the Government on Digital's GSA Schedule of over $3,000,000. If this same price advantage is achieved from other Schedule 70 vendors, over $100,000,000 in savings would be realized by the Government.

What additional risks would the Government assume by using such a modified commercial contract? We believe -- none. GSA would still have a right to review commercial practices including volume discounts and allowances which establish Digital's commercial practice. GSA could also invite non-schedule vendors to compete against schedule vendors in the interest of achieving maximum competition and lowest prices. Beyond the two terms proposed to be modified, no other changes are required to achieve a commercial-like procurement process.

Summary and Recommendations

In Digital's judgment, the most important outcome of these hearings would be the introduction of legislation, applicable to all Government agencies, that establishes the presumption that, as a general rule, a commercial solution can be found for any Government information system requirement. The legislation would spell out the conditions under which an agency could take exception to the commercial solution and procure a custom-built product. The wording of exception guidelines would closely approximate the six exceptions to full and open competition found in the Competition in Contracting Act.

Second, the legislation would outline how requirements should be expressed. Insofar as possible, requirements should always be stated in functional terms. Any other more specific statement of requirements, such as performance specifications or design specifications, would require higher level review and would follow current rules in the Federal Acquisition Regulations (FAR) for determinations and findings.

Third, the legislation would direct the National Institute of Science and Technology (NIST) to review the Government's Federal Information Processing Standards publications (FIPS Pubs) to determine which standards conform to user interface criteria. Those that do not would be considered for recession. Remaining standards would also be reviewed for currency and completeness and any possible conflict with emerging standards. NIST would also be required by law to issue government-wide determinations and findings as the basis for emerging standard conflict resolution.

Finally, We need the vigorous support of the Congress in encouraging GSA to pursue this commercial alternative by establishing a test program as part of the FY90 MAS program and by appointing a GSA Schedule program manager. We are available to assist in whatever capacity to demonstrate the soundness of our proposal and to join with others in industry and Government in realizing the objective of using commercial acquisition of commercial products by the Government.

Very truly yours,

Harvey L Weiss

Harvey L. Weiss
Vice President
Federal Systems Group

cc: Bill Luke
Warren Reese